S. HRG. 98-121

FLOOD, CRIME AND RIOT INSURANCE

HEARING

BEFORE THE

SUBCOMMITTEE ON INSURANCE

OF THE

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS UNITED STATES SENATE

NINETY-EIGHTH CONGRESS

FIRST SESSION

ON

S. 460

TO AMEND THE NATIONAL FLOOD INSURANCE ACT OF 1968

S. 895

TO AUTHORIZE APPROPRIATIONS FOR STUDIES UNDER THE NATIONAL FLOOD INSURANCE ACT OF 1968 FOR THE FISCAL YEARS 1984 AND 1985, TO EXTEND THE AUTHORIZATION FOR FLOOD INSURANCE, AND FOR OTHER PURPOSES

APRIL 8, 1983

Printed for the use of the Committee on Banking, Housing, and Urban Affairs

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FLOOD, CRIME, AND RIOT INSURANCE

FRIDAY, APRIL 8, 1983

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
SUBCOMMITTEE ON INSURANCE,
Washington, D.C.

The subcommittee met at 9:30 a.m. in room 538 of the Dirksen Senate Office Building, Senator Chic Hecht, chairman of the subcommittee, presiding.

Present: Senators Hecht, D'Amato, and Hawkins.

Also present Senator Eagleton.

OPENING STATEMENT OF SENATOR HECHT

Senator HECHT. The hearing of the Subcommittee on Insurance will come to order. The Chair wishes to recognize my distinguished colleague from the State of Missouri, Mr. Eagleton.

The Senator has come before us today to comment on his bill, S. 460, which seeks to amend the National Flood Insurance Act of 1968. I would just like to remind the Senator that I was born and raised in Cape Girardeau, Mo., and I attended college at Washington University in St. Louis. I still have some family living in that part of the country, so the Senator can be assured that I will listen closely to his comments.

In addition to the comments we will hear on S. 460, our primary reason for meeting here today is to hear testimony on the reauthorization of the national flood insurance, crime insurance, and riot reinsurance programs. At the request of the administration, I introduced S. 895 which contains their proposals for reauthorization of these three Federal programs.

[Copy of S. 460 and S. 895 follow:]

II

98TH CONGRESS
1ST SESSION

S. 460

To amend the National Flood Insurance Act of 1968.

IN THE SENATE OF THE UNITED STATES

FEBRUARY 3 (legislative day, JANUARY 25), 1983

Mr. EAGLETON introduced the following bill; which was read twice and referred to the Committee on Environment and Public Works

FEBRUARY 24 (legislative day, FEBRUARY 23), 1983

Committee discharged; referred to the Committee on Banking, Housing, and Urban Affairs, by unanimous consent

---

A BILL

To amend the National Flood Insurance Act of 1968.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That section 1305(c) of the National Flood Insurance Act of 1968 is amended by adding at the end thereof the following flush sentence:

"In addition, notwithstanding the provisions of section 1315, the Secretary may make flood insurance available for individual properties in other States or areas or subdivisions thereof where the Secretary finds that—

"(A) the failure of participation is not attributable to the person making application for the insurance;

"(B) such person has made a good faith effort to encourage participation;

"(C) such person agrees to meet such terms and conditions as would be applicable in the case of a property located in a participating area; and

"(D) the property was constructed prior to the identification of the area as having special flood hazards.".

II

98TH CONGRESS
1ST SESSION

S. 895

To authorize appropriations for studies under the National Flood Insurance Act of 1968 for the fiscal years 1984 and 1985, to extend the authorization for flood insurance, and for other purposes.

IN THE SENATE OF THE UNITED STATES

MARCH 23 (legislative day, MARCH 21), 1983

Mr. HECHT (by request) introduced the following bill; which was read twice and referred to the Committee on Banking, Housing, and Urban Affairs

---

A BILL

To authorize appropriations for studies under the National Flood Insurance Act of 1968 for the fiscal years 1984 and 1985, to extend the authorization for flood insurance, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

AUTHORIZATION OF APPROPRIATIONS FOR STUDIES

SECTION 1. Section 1376(c) of the National Flood Insurance Act of 1968 is amended to read as follows:

"(c) There are authorized to be appropriated for studies under this title not to exceed $50,582,000 for fiscal year

1984, and such sums as may be necessary for fiscal year 1985.".

EXTENSION OF FLOOD INSURANCE AUTHORITIES

SEC. 2. The National Flood Insurance Act of 1968 is amended—

(1) by striking out "May 20, 1983" in section 1319 and inserting in lieu thereof "September 30, 1985";

(2) by striking out "May 20, 1983" in section 1336(a) and inserting in lieu thereof "September 30, 1985"; and

(3) by striking out "within fifteen years of such date" in section 1360(a)(2) and inserting in lieu thereof "by September 30, 1987".

CRIME AND RIOT INSURANCE

SEC. 3. Section 1201(b)(1) of the National Housing Act is amended by striking out "May 20, 1983" and inserting in lieu thereof "September 30, 1983".

TECHNICAL AMENDMENTS

SEC. 4. (a) Section 1370(a)(6) of the National Flood Insurance Act of 1968 is amended to read as follows:

"(6) the term 'Director' means the Director of the Federal Emergency Management Agency.".

(b) Section 3(a)(6) of the Flood Disaster Protection Act of 1973 is amended to read as follows:

"(6) 'Director' means the Director of the Federal Emergency Management Agency.".

(c) Section 1304(a) of the National Flood Insurance Act of 1968 is amended by striking out "Secretary of Housing and Urban Development" and inserting in lieu thereof "Director of the Federal Emergency Management Agency".

(d) Except for any reference to the Secretary of a Department other than the Department of Housing and Urban Development—

(1) wherever the term "Secretary" is used in the National Flood Insurance Act of 1968 or in the Flood Disaster Protection Act of 1973, it is changed to the term "Director"; and

(2) wherever the term "Secretary's" is used in the National Flood Insurance Act of 1968 or in the Flood Disaster Protection Act of 1973, it is changed to the term "Director's".

(e) Section 15(e) of the Federal Flood Insurance Act of 1956 is amended by striking out "Secretary" the first and third places it appears and inserting in lieu thereof "Director of the Federal Emergency Management Agency".

(f) Section 1201(c) of the National Housing Act is amended by adding at the end thereof the following:

"(c) As used in this title, the term 'Director' means the Director of the Federal Emergency Management Agency.".

(g) Title XII of the National Housing Act is amended by striking out the term "Secretary" wherever it appears and inserting in lieu thereof "Director".

(h) Section 1340(a)(2) of the National Flood Insurance Act of 1968 is amended by striking out "officers and employees of the Department of Housing and Urban Development, and".

(i) Section 1232(2) of the National Housing Act is amended by striking out "officers and employees of the Department of Housing and Urban Development, and".

(j) Section 1247 of the National Housing Act is amended by inserting "of the Secretary of Housing and Urban Development" after the second parenthetical phrase.

I am very pleased that we have with us today several witnesses who will be offering their comments and recommendations for the future of these insurance programs. In looking over the list I see that our guests represent National and State Government, academia, and the private sector. The record we establish today will assist us on this subcommittee and our colleagues on the full Banking Committee as we formulate reauthorizing legislation for these programs.

Senator D'Amato, do you want to make a statement?

Senator D'AMATO. Yes, Senator, I will, but I will withhold until Mr. Eagleton has finished.

Senator HECHT. I would now yield the floor to Senator Eagleton.

STATEMENT OF THOMAS F. EAGLETON, U.S. SENATOR FROM THE STATE OF MISSOURI

apologize to you and Senator D'Amato for my tardiness. I hope I have not unduly inconvenienced the committee and I acknowledge your significant Missouri connection. In fact, the witness that I will introduce when I conclude my testimony, State Senator Jack Gannon from Missouri, is from Jefferson County, Mo., which, as you'll recall from your Missouri days, is just a shade north of Cape Girardeau County. So in a sense it's old home week here today.

[The complete statement follows:]

STATEMENT OF SENATOR THOMAS F. EAGLETON

Mr. Chairman, I appreciate the Subcommittee's scheduling this early hearing. I do not intend to take much of the Subcommittee's time, but instead will ask that a statement I made in the Senate describing the provisions of S. 460 be made part of the record.

Mr. Chairman, I want to emphasize three things about this modest bill:

(1) The authority which S. 460 provides to sell flood insurance on an individual basis is discretionary with the Administrator.

(2) The Administrator may use his discretion only in those cases where he is persuaded that legal or political impediments make community-wide participation in the program unlikely.

(3) The authority to make individual sales is further circumscribed by the condition that only homes, farms, and businesses which were located in the flood plain at the time the community was notified of its flood-status would be eligible for individual insurance. In short, this bill in no way would encourage new construction in flood hazard areas.

Mr. Chairman, as a general matter, I support the objectives of the flood insurance program. But, theories hatched in Washington don't always fit with facts at the local level. In that situation, the rational thing to do is to refine the theory. The Administrators of this program, however, stubbornly ignore the facts and go right on insisting they will pound square pegs into round holes no matter how many innocent people get hurt.

My bill is an effort to change that situation. I believe this measure will advance the goal of expanded flood insurance coverage while, at the same time, relieve thousands of helpless property owners from the unfair sanctions they are now enduring.

[From the Congressional Record, Feb. 3, 1983]

By Mr. EAGLETON:

S. 460. A bill to amend the National Flood Insurance Act of 1968; to the Committee on Environment and Public Works.

FEDERAL FLOOD INSURANCE PROGRAM

Mr. EAGLETON. Mr. President, today I am introducing a bill to bring a little commonsense and justice to the operation of the Federal flood insurance program.

Since its inception in 1968, this program has operated on an all or nothing basis. Either an entire community agreed to participate by virtue of adopting the federally mandated building restrictions or nobody, however willing they may be as individual property owners, would be allowed to purchase the subsidized insurance.

Matters became much worse when, in 1973, Congress made participation in the program obligatory. As a result of that change, residents of a nonparticipating community are not only denied the right to buy flood insurance but they are further penalized by being denied any form of Federal assistance for repair of a building damaged in a flood.

Mr. President, the justification for these extreme measures is to persuade communities not to build in flood-hazared areas and to look to tax-funded disaster programs to bail them out when the waters rise. I generally support that objective, but within limits of reason.

It is one thing to penalize property owners who freely reject the protection of flood insurance. It is quite another matter to heap penalties on homeowners and businessmen who desperately want to join the program, but are legally unable to adopt the required building ordinance or politically unable to persuade a majority upon high ground to see the wisdom of accepting Federal land use dictates.

To bureaucrats surveying the world from the towers of the FEMA building in Washington, land use controls are simple good management tools. But to many landowners and their State and local representatives out where real people live, Federal land use controls are anathema and an attack on private property rights.

You do not have to agree with that view. You only have to know it is very real and very strong in many areas of this country. Typically, residents of a flood plain constitute a small minority of the community which must adopt the Federal guidelines. Not surprisingly, their efforts often fail.

In my State of Missouri, there is an added legal complication. Unincorporated communities are prohibited by State law from adopting zoning and building ordinances. Numerous attempts have been made to change that law and all have failed. Yet, hundreds of these small communities have been told by the Federal Government. "No matter, you either find a way to do it or suffer the penalties."

Mr. President, the bill I am introducing today would authorize the administrator of the flood insurance program to make exceptions to the present all-or-nothing rule when circumstances of the kind I have described are present.

In those cases, it would permit insurance to be sold on an individual basis to homeowners and businessmen who agree by contract to comply with relevant building restrictions. This is how most other Government loan programs work. There are always conditions attached to SBA, VA, or FmHA loans and, contrary to the claims of past flood insurance administrators it does not take an army of bureaucrats to enforce. Those contractual loans are essentially self-enforcing. A recipient who violates the agreed-to terms loses his loan or suffers foreclosure. I would work precisely the same way with individual sales of flood insurance—a purchaser who violated the building restrictions would simply find his policy invalidated.

There is one point on which I would agree with the Federal insurance agency and that is, we should do nothing which might encourage new construction in flood-hazard areas. Accordingly, my bill limits the right of individual purchase of flood insurance to those homes and businesses which were in place prior to the time their community was officially notified of its flood status.

Mr. President, my bill is a modest effort to redress the injustice of the present, rigid flood insurance program. It is premised on the idea that the Federal Government should not inflict penalties on individuals for situations beyond their control. No purpose can be served by continuing to kick around property owners whose only offense was political impotence. To the contrary, the objectives of this program should be to bring as many property owners as possible—by whatever means—into compliance with sound flood plain practices. That is what my bill provides.

Mr. President, I ask that the text of the bill be printed at this point in the RECORD.

There being no objection, the bill was ordered to be printed in the Record, as follows:

S. 460

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That section 1305(c) of the National Flood Insurance Act of 1968 is amended by adding at the end thereof the following flush sentence:

"In addition, notwithstanding the provisions of section 1315, the Secretary may make flood insurance available for individual properties in other States or areas or subdivisions thereof where the Secretary finds that—

"(A) the failure of participation is not attributable to the person making application for the insurance;

"(B) such person has made a good faith effort to encourage participation;

"(C) such person agrees to meet such terms and conditions as would be applicable in the case of a property located in a participating area; and

"(D) the property was constructed prior to the identification of the area as having special flood hazards."

Senator EAGLETON. Now, if I may, Mr. Chairman, could I call to the witness table State Senator Gannon from Missouri.

Senator HECHT. Fine.

Senator EAGLETON. State Senator Gannon, as I say, is from Jefferson County, Mo., somewhat south of St. Louis and a little bit north of Cape Girardeau. He has in the Missouri Legislature interested himself in this subject and worked very assiduously at it. I think he can bring us a local perspective that would be of interest to this committee and I'll yield to him at this time, Mr. Chairman.

Senator HECHT. Thank you very much.

STATEMENT OF JACK GANNON, STATE SENATOR, STATE OF MISSOURI

Mr. GANNON. Mr. Chairman, would you like me to hand you my material?

Senator HECHT. Please.

[The complete statement follows:]

Also submitted for the record, statement of Emory Melton, State Senator, State of Missouri.

Statement by Missouri State Senator Jack Gannon
Before the U.S. Senate Banking & Urban Affairs Committee,
Subcommittee on Insurance

April 8, 1983, 9:30 a.m.

Mr. Chairman, members of the Committee, my name is Jack Gannon. At the present time I am in my ninth year as State Senator representing Jefferson County, adjoining St. Louis County to the south along the Missouri and Mississippi rivers. I live in DeSoto, Missouri which is the population center of the United States of America.

For 30 years I have been in the grocery and retail business. I am here today in support of Senator Eagleton's proposal to amend the National Flood Insurance Act. Jefferson County has a population of 150,000 people. Perhaps 10,000 people live in the actual flood plain area. I want those 10,000 people who want flood insurance to have it, but I do not want to penalize the other 140,000. Mr. Chairman, I am very much concerned about the industry and port development in our county. With the way it is used now the flood insurance program will virtually stop industrial growth and cost millions of dollars in property value. All of our industrial parks are individually located in the flood plain area. One example -- Missouri Pacific Railroad has a car shop in my hometown of DeSoto, Missouri employing about 350 people. If the car shops were destroyed tomorrow by any cause to the extent of 50% or more of its value, we would lose a factory because it couldn't be rebuilt. In order to comply with FEMA standards we have to build the car shops 10 feet high in the air. Mr. Chairman, there are many people who do not want to have the federal government deciding what they can or cannot do. If they choose to abide by FEMA regulations they should have the right to buy insurance. On the other hand, they should not be forced to comply by FEMA if they do not want the insurance. Mr. Chairman, the bureaucracy when they get in your district get to be dictators.

(Example)

APRIL 8, 1983

STATEMENT OF SENATOR EMORY MELTON

MR. CHAIRMAN, AND MEMBERS OF THE COMMITTEE:

MY NAME IS EMORY MELTON. AT THE PRESENT TIME, I AM IN MY ELEVENTH YEAR AS A MISSOURI STATE SENATOR REPRESENTING ELEVEN RURAL COUNTIES OF ONE HUNDRED AND EIGHTY THOUSAND PEOPLE IN THE OZARKS MOUNTAINS REGION OF SOUTHWEST MISSOURI.

FOR THIRTY-FIVE YEARS, I HAVE PRACTICED LAW AND CURRENTLY PUBLISH FOUR NEWSPAPERS.

THIS STATEMENT IS PRESENTED FOR YOUR CONSIDERATION IN SUPPORT OF SENATOR EAGLETON'S PROPOSAL TO AMEND THE NATIONAL FLOOD INSURANCE ACT.

MY EXPERIENCE WITH THE ACT GOES BACK SEVERAL YEARS TO A TIME WHEN THE FEDERAL BUREAUCRAT FROM THE KANSAS CITY OFFICE OF FEMA CAME TO AT LEAST THREE TOWNS IN MY SENATORIAL DISTRICT (INCLUDING MY HOME TOWN OF CASSVILLE) SEEKING TO EUCHRE THE CITY INTO ADOPTING THE FEDERAL FLOOD INSURANCE PROGRAM. WHEN THE CITY FATHERS REFUSED TO PASS ORDINANCES ADOPTING THE SAME, HE TOLD THE PRESS AND NEWS MEDIA WE WERE "A BUNCH OF REDNECKS." THIS REMARK INSURED THAT THE CITIES WOULD NOT ADOPT THE PLANS.

IN CITIES WHICH HAVE ADOPTED THE ORDINANCES, PLEASE CHECK AND SEE HOW MANY PROPERTIES ARE ELIGIBLE AND HOW FEW HAVE PURCHASED FLOOD INSURANCE. THE FIGURES HERE IN MISSOURI ARE VERY REVEALING.

DURING THE HOLIDAY SEASON AT THE END OF 1982, WE HAD SOME DEVASTATING ~~DEVASTING~~ FLOODS IN MISSOURI, INCLUDING ONE AT THE TOWN OF WAYNESVILLE WHICH HAD ELEVEN HUNDRED PERSONS LIVING IN DESIGNATED AREA FLOOD

ZONES. IN THE ENTIRE TOWN OF WAYNESVILLE THERE WERE TWENTY-TWO FLOOD INSURANCE POLICIES. FROM MY OBSERVATION THIS WAS REPRESENTATIVE OF THE PERCENTAGE OF UTILIZATION OF THIS PROGRAM THROUGHOUT THE STATE.

THERE CAN BE NO QUESTION UNDER THE PROVISIONS OF THE RULES AND REGULATIONS PROMULGATED TO IMPLEMENT THE ACT ~~BUT WHAT~~ THAT AN ORDINANCE COVERS AN ENTIRE AREA DESIGNATED AS A "FLOOD PLANE." THE REQUIREMENTS FOR ADDITIONS TO EXISTING STRUCTURES OR NEW BUILDING IN THE "FLOOD PLANE" ARE HARSH AND, IN MANY INSTANCES, WOULD, AS A PRACTICAL MATTER, PROHIBIT EXPANSION OF EXISTING INDUSTRIES IN THOSE AREAS.

IN THE CITY OF SPRINGFIELD, WHICH HAS A POPULATION OF APPROXIMATELY ONE HUNDRED AND TWENTY-FIVE THOUSAND PERSONS, THE CITY COUNCIL, SEVERAL YEARS AGO, REFUSED TO ADOPT "FLOOD PLANE" REGULATIONS AND GAVE AS THEIR REASON THEREFOR THAT THOSE REGULATIONS WOULD DEVASTATE SOME THIRTY MILLION DOLLARS' WORTH OF INDUSTRIAL PROPERTIES IN THE JORDAN CREEK VALLEY IN THE CITY.

I OWN A PRINTING AND BOOKBINDING PLANT IN CASSVILLE WHICH I HAVE ENLARGED FOUR TIMES IN THE LAST TWENTY YEARS. IT IS SITUATED IN A FLOOD ZONE. I AM WILLING TO TAKE THE RISK AND DO NOT WANT FLOOD INSURANCE. THE CITY OF CASSVILLE HAS REFUSED TO ADOPT SUCH AN ORDINANCE. I AM PLEASED THAT THEY HAVE.

BUT, WHAT ABOUT MY NEIGHBOR, WHO OPERATES A NEARBY PLACE OF BUSINESS AND WOULD LIKE TO PURCHASE FLOOD INSURANCE. HE HAS A BUSINESS WHICH COULD BE DEVASTED BY A FLOOD AND WOULD BE WILLING TO ABIDE BY THE PROVISIONS OF SUCH AN ORDINANCE. HE IS BEING DENIED THE RIGHT TO BUY FLOOD INSURANCE.

ISN'T IT A MATTER OF SIMPLE JUSTICE AND COMMONSENSE THAT SENATOR EAGLETON'S PROPOSAL BE ADOPTED AND THIS WOULD PERMIT MY NEIGHBOR TO BUY FLOOD INSURANCE AS LONG AS HE IS WILLING TO ADOPT

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THE REQUIREMENTS IMPOSED BY FEMA FOR THE PURCHASE OF THAT INSURANCE. WHY SHOULD WE SINGLE HIM OUT AND DENY INSURANCE TO HIM SIMPLY BECAUSE HIS NEIGHBORS DON'T WANT IT AND HIS CITY COUNCIL WILL NOT ADOPT THE INSURANCE?

THE SAME ARGUMENT IS APPLICABLE TO THE COUNTIES IN THE STATE OF MISSOURI WHICH WOULD COVER THE UNINCORPORATED PORTIONS OF THE STATE. LOGICAL ARGUMENT TO COUNTERACT THIS POSITION IS THAT FEDERAL AID SHOULD NOT BE EXTENDED TO THOSE JURISDICTIONS WHICH DO NOT ELECT TO ADOPT "FLOOD PLANE" REGULATIONS FOR ALL PROPERTIES WITHIN THAT JURISDICTION. THE FALLACY OF THIS ARGUMENT IS THAT PROPERTY OWNERS WITHIN THE AREA, AS SHOWN BY EXPERIENCE, WHO PURCHASE FLOOD INSURANCE ARE FEW IN NUMBER; AND, CONSEQUENTLY, THE GOVERNMENT FAILS TO ACHIEVE ITS PURPOSE UNDER THE PRESENT PLAN OF OPERATION.

I WOULD URGE THE MEMBERS OF THIS COMMITTEE TO VOTE FAVORABLE ON THE PROPOSAL OF SENATOR EAGLETON.

Senator HECHT. Thank you.

Senator D'Amato, do you have any questions?

Senator D'AMATO. Well, let me ask you, isn't it possible for your State to enact legislation that would permit your local communities to participate in this program?

Mr. GANNON. Just recently, Senator, we had legislation introduced in the Missouri Senate that would allow the county court to adopt ordinances whereby they could set rules and regulations that would comply with the FEMA standards for Federal flood insurance. The problem that we've had is a lot of our people do not live in the flood plain area. Maybe 5 percent of these people live in that area. And therefore, our people are opposed to it, the fact that they would have to live by the rules and regulations which almost make it prohibitive to build any structure whatsoever.

What I would like to see is that these people who actually live in the flood plain area be allowed to purchase insurance. Now, we did pass legislation a few years ago that all the counties along the Mississippi and Missouri Rivers could comply with FEMA Federal regulations and adopt the Federal flood insurance program. We gave that authority to the counties several years ago.

Just recently, FEMA came in and said unless the whole State of Missouri allows legislation to be passed whereby they can set up the rules and regulations of FEMA Government, we're going to cancel you out of the insurance. I fought this very hard and wanted to put it to the vote of the people and FEMA said they wouldn't take it, and so what happened in Jefferson County was voted into it but the rest of the county now had it by the vote of the people. So all the counties along the Mississippi and Missouri Rivers, the county court has the right to adopt ordinances to comply with the Federal Government.

What I'm saying is the rules and regulations set out by the Federal Government virtually cover every inch of Jefferson County, although we're not in the flood area. And also, the rest of the State, the way it is at the present time, would have to have an election or referendum to get the flood insurance and that will not take place because 95 percent of the people do not live in the flood plain area. They're not going to vote for it. So that's the reason we need Senator Eagleton's legislation more than ever before. Then we would make the insurance available to the people that actually needed it and wanted it.

Now if they don't want it, that's fine. Then they will not receive it but if they want it then they have to live up to the rules and regulations set up by FEMA. I don't think there's anything wrong with that.

Senator EAGLETON. One specific example briefly, Senator, if I may. to illustrate this. In north St. Louis along the Mississippi River, there's a county called Lincoln County. Congressman Hungate used to be from Lincoln County. These aren't exact figures. These are recollections. They had a referendum countywide. Roughly about 10 percent of the property owners were in the flood plain adjacent to the river. Of the other 90 percent, the land started to rise totally without any flood risk. When the election results came in, roughly speaking, they were about 90 to 10. Those on high ground voted virtually unanimously, saying they didn't want any part of that program, and those that were in the flood plain area, roughly 10 percent, virtually unanimously voted yes. Yet, because of that result, the poor folks down in the flood-prone area were helpless. They couldn't get into the program and wanted to and cast their individual votes to get into it, but their neighbors on the high ground said no.

Senator HECHT. Senator Gannon, in a few minutes our next witness is Jeff Bragg and I will address this question to him after his testimony and we'll let him address it.

Mr. GANNON. Thank you, Senator, for your kindness.

Senator HECHT. Anything else?

Senator D'AMATO. No.

Mr. GANNON. Senator Eagleton can explain my views much better than I.

Senator HECHT. I hope you will stick around for the rest of the testimony.

Mr. GANNON. I would love to. Thank you for your courtesy you've shown this morning. I might comment that a hearing on the Federal level on Friday morning is fantastic. It shows you people are out working.

Senator HECHT. You know everyone from Missouri is taught and raised to work hard.

Mr. GANNON. That's right. Thank you.

Senator HECHT. Mr. Jeff Bragg, would you come up, please. Thank you for coming today. We will now hear your testimony.

One minute, Mr. Bragg. Senator D'Amato.

OPENING STATEMENT OF SENATOR D'AMATO

Senator D'AMATO. Thank you very much, Mr. Chairman.

Mr. Chairman, today we are once again here to discuss the program of the Federal Insurance Agency. As we all know, the Federal crime insurance program was enacted in 1970 to help those small businesses and homeowners unable to purchase or unable to afford prohibitively expensive crime insurance coverage. This program by its nature was never intended to be self-sustaining. It was designed to serve those areas where critical crime insurance availability problems exist.

In 1981 we reauthorized the Federal crime and riot insurance for 1 year and asked that a study be performed to clarify the need for this insurance and enable the committee to make its recommendations. To date, I've seen no such report.

Last year when we marked up the housing bill, which unfortunately was never enacted, Senator Dodd and I offered an amendment which would have reauthorized Federal crime and riot insurance until September 30, 1984, and September 30, 1985, respectively. This amendment was approved by a vote of 10 to 5 of this committee. Therefore, we are again forced to review this worthwhile and cost-effective program.

We are being told by the administration that it wants to eliminate Federal riot and crime insurance because they are primarily utilized in only a few States. New York, may I add, is a State that has the highest number of policyholders. Mr. Bragg, the Administrator of the Federal Insurance Agency, has been quoted in the March 1983 issue of the National Underwriter as saying, "This program is not of national proportions but is used in only 2 or 3 States." He goes on to state that "Members of Congress who sit on the House and Senate Banking Committees come from the States such as New York with the biggest stake in the Federal program and are not interested in eliminating the program," and he's absolutely correct.

Let's look at the facts. First, over 30 States have asked to be included in this program to date, including two within the past year—California and Louisiana. Two GAO audits have shown that people in the eligible areas did not know that the program existed and had they known they would have purchased this insurance. What has the agency done to make known the existence of this insurance program or have they deliberately failed to inform possible purchasers or sought methods encouraging people to participate in this program?

I would suggest that it would probably be both, having read just a few moments ago this article which states that even if Congress does not seek to eliminate the program that the Administrator will use other devices to eliminate the program.

I would suggest that if that word gets out, then the Administrator might have a great deal of difficulty in dealing with Congress on this subject.

In any event, by passing the D'Amato-Dodd amendment last year, the committee requested a study from the Comptroller General on the marketing of crime insurance to residents of high crime urban areas. Since the 1982 housing bill was never enacted, this study was never undertaken and I will once again, independently of any legislation by this committee, Mr. Chairman, request a total and complete study on this issue because I think it's imperative

that we have this information so that we can make our decisions intelligently.

After a close review of the enabling statute I'm hopeful that we'll be able to get this information this year. Last year I asked the American Insurance Association whether they knew of any companies that were prepared to offer crime insurance in New York City at affordable rates. Their answer was that no private insurance company is able to provide crime insurance to high risk insurers in high crime areas at affordable rates.

If this program were ended, it would mean that small, high risk businesses in high crime urban areas would not be financially able to purchase insurance protection against crime losses. Thus, the elimination of this insurance would be particularly counterproductive to our urban areas which I believe need every assistance for revitalization and renewal so they can do it on their own.

Indeed, the testimony of the State Insurance Commissioner will indicate substantial areas have dropped out of the crime insurance program because of the beneficial impact of that program—recreating an attitude and an atmosphere where neighborhoods through their own initiative were able to rebuild so that they no longer qualify. It would seem to me that the seed money, so to speak, to make that available only came and would only have been available as a result of this crime insurance. It seems incongruous to me that there are those people who believe it is inappropriate to subsidize small businesses in those areas of the country where Federal crime insurance programs are being heavily utilized. Couple that with the fact that much of the crime created in these areas comes as a direct result of inadequate Federal programs dealing with the migrations of millions of poor aliens who come into these areas and create many of the problems.

This position is advocated by the same people who advocate that taxpayers subsidize flood losses with the Federal flood insurance program. I submit there is no difference between a rural or suburban taxpayer subsidizing crime insurance losses in urban areas than an urban or even landlocked taxpayer subsidizing flood losses in suburban or rural areas.

Now, it may be that we have a greater constituency and so consequently you don't dare bring out the elimination of flood insurance, nor does this Senator suggest that. Surely, when one considers the cost of flood insurance, which I support and I'll continue to support, it's at least $1.5 billion and the crime insurance program is at an approximate annual cost of $20 million pales in comparison, and indeed is the whipping boy—and I would suggest once again that I resent those who come in and point to New York in particular and use it as the whipping boy.

So, Mr. Chairman, I thank you for giving me the opportunity of making these points because I think it is of vital importance that we provide the annual appropriation to see to it that this program continues.

Senator HECHT. Thank you, Senator. And on that note, the Honorable Jeff Bragg.

STATEMENT OF MR. JEFFREY BRAGG, ADMINISTRATOR, FEDERAL INSURANCE ADMINISTRATION, ACCOMPANIED BY JIM TAYLOR

Mr. BRAGG. Thank you, Mr. Chairman. I would like to present my testimony this morning, and some of the questions raised by the Senator from New York will be answered in my testimony. If I fail to answer them, I hope that he will raise them when I've completed my statement.

Senator D'AMATO. You can be assured of that.

Mr. BRAGG. I'm here today with Jim Taylor, who is with the Insurance Support Services Office of the Federal Insurance Administration.

[The complete statement follows:]

STATEMENT BY JEFFREY S. BRAGG, ADMINISTRATOR, FEDERAL INSURANCE ADMINISTRATION, FEDERAL EMERGENCY MANAGEMENT AGENCY

I am Jeffrey S. Bragg, Administrator of the Federal Insurance Administration (FIA), which is one component of the Federal Emergency Management Agency. I am here before the committee today to address the three insurance programs of the Federal Insurance Administration; namely, the Federal riot reinsurance program, the Federal crime insurance program, and the national flood insurance program, all three of which respond to losses resulting from manmade and natural occurrences. The three programs provide payments to those who have protected themselves against the possibility of loss by purchasing policies of insurance.

The Federal riot reinsurance program provides reinsurance against the peril of riot and civil commotion to 16 private property insurance companies in fifteen States, a very substantial decline from 300 companies insured in the 1980-81 contract year and 98 in the 1981-82 contract year. Five hundred million dollars of Federal riot reinsurance is in force compared with thirty-five billion dollars the year before.

The Federal crime insurance program provides burglary and robbery insurance to approximately 59,000 residents and businesses in 27 States and the District of Columbia, Puerto Rico and the Virgin Islands. This reflects a decline of approximately 20,000 policies over the past two years.

Eligibility for burglary insurance coverage is conditioned upon the insured's compliance with protective requirements designed to deter crime losses. There are approximately 43,000 residential and 16,000 commercial policies in force and insurance in force totals $477,051,000 as of February 28, 1983.

Because FEMA's authority to write new insurance policies under these programs expires on May 20, 1983, Congress is faced with the question of whether to extend this authority. For the reasons which follow, this administration recommends that the current statutory authority for the Federal riot reinsurance program and the Federal crime insurance program be extended only until September 30, 1983, at the latest, and that the runoff of the business on existing policies be administered under the provisions of the current statute which requires no change.

The Federal riot reinsurance program has, fortunately, not been faced with property losses of the magnitude which were suffered by the private insurance market during the 1960's. Since the program was designed to be self-supporting, premiums have always exceeded losses. However, the reserves in the national insurance development fund have been totally depleted by the Federal crime insurance program, even though riot reinsurance premiums were increased beginning with the 1981-82 contract year.

With reinsurance coverage readily available in the private sector, there has been a dramatic decline in the number of companies purchasing Federal riot reinsurance.

In view of the diminished need for Federal riot reinsurance, we recommend that it not be extended beyond September 1983.

The Federal crime insurance program was legislated by Congress after a study made by the Federal Insurance Administration in 1970 indicated that availability and/or affordability problems existed in major urban areas. This program, which in 1970 was grafted onto the 1968 legislation authorizing the Federal riot reinsurance program, has been primarily financed through the national insurance development fund (NIDF) into which the premiums from both Federal riot reinsurance and crime insurance are deposited. Substantial premium increases and policy revisions have

been introduced as part of our Federal Insurance Administration's goal of improving the underwriting of this program through protective device upgrading and more realistic rating of especially vulnerable risks. These measures have significantly reduced the overall loss ratio from three dollars of losses per one dollar of premium down to two dollars of losses per one dollar of premium. Nevertheless, the Federal crime insurance program while making affordable crime insurance available, as provided by the authorizing statute has cost $167,000,000 more than the premiums received. The deficit has been financed by $124,000,000 in excess premiums from the Federal riot reinsurance program and by $43,000,000 in borrowings from the general funds of the Treasury. At current premium levels, and even allowing for future increases, FEMA sees little chance of repaying these borrowings without appropriations. (Given the relatively small number of insureds in the program, approximately 79 percent of whom reside in the States of Florida, Pennsylvania, Massachusetts, New Jersey, and New York, and the lack of response to public awareness efforts, we believe that the authority for the writing of new policies under this program, which expires on May 20, 1983, should be extended only to September 30, 1983.) New York State, for example, accounts for nearly 35,000 policies, constituting 59 percent of all policies. Considering that such a number represents less than one-half of one percent of the population of the greater New York City area, clearly it is not beyond the means and resources of New York State to resolve the insurance needs of its citizens without a Federal program. FIA strongly believes that the availability problems of relatively small number of insureds who have felt a need for this program can be better addressed at the State level, where, since the 1800's, the insurance regulatory functions of the Nation have been conducted through State insurance departments.

The largest of the three programs is the national flood insurance program which has nearly 2,000,000 policies in force protecting dwellings and/or contents from loss by flood. The availability of flood insurance in a community is dependent upon the community's adopting and enforcing flood plain management measures. The responsibility within FEMA for administering the flood plain management aspects of the program is assigned to the office of State and local programs and support. The deputy associate director of that office, Mr. Dave McLoughlin is here today and will answer questions on those aspects of the program in a separate panel. Individual availability of insurance is conditional upon the insured residing or doing business within one of the 17,351 communities participating in the program as of January 31, 1983. Of these communities, 8,600 are in the emergency program, which requires a lesser degree of flood plain management measures by the community, and 8,751 are in the regular program which requires more extensive flood plain management measures in accordance with identified base flood elevations in the areas of special flood hazard. It is significant that 84 percent of all policyholders are insured in the regular program. Insurance coverage in force nationwide amounts to approximately one hundred five billion dollars.

We believe that continuation of the NFIP is clearly in the interests of the Nation and that its authority should be extended beyond the May 20, 1983 expiration date which all three programs face. In order to assure better program continuity, we recommend an extension of the national flood insurance program until September 30, 1985. Many steps have been taken to improve the efficiency of this operation with a more actuarially based premium rate schedule, revisions in the policy coverages, tighter claims practices, and improved overall monitoring of the growing program. For example, premiums now reflect wave height in the case of new construction if coastal high hazard V-zones. A newly developed slide rule for determining premiums makes the rating process far simpler for insurance agents and insureds and a new "solo adjuster" arrangement, by which the same adjuster adjusts flood and wind losses, eliminates duplication of effort and delay in claim payments. Moreover, as of October, 1983, no insurance will be available for new construction in undeveloped portions of coastal barriers in accordance with the Coastal Barrier Resources Act of 1982.

With these long overdue rate increases, which were the first to be applied to the program since the beginning of the program, we are moving toward one of our main goals, that of bringing the program to an actuarially sound basis by 1988. The Federal Insurance Administration is encouraging greater private insurance industry participation in the national flood insurance program and has initiated discussions which could lead to eventual involvement of the insurance industry in administering some aspects of the national flood insurance program. Such a step will greatly assist us in our goal of increasing the number of policies sold, thus broadening the premium base and helping us keep premiums within the means of our insured.

While the Federal Insurance Administration is anxious to increase the number of policyholders, in the National Flood-insurance program we are opposed to S. 460, a bill introducted by Senator Eagleton. This bill would permit the purchase of flood insurance by certain residents of non-participating communities, which have failed to adopt flood plain management measures.

S. 460 would encourage communities to withdraw from the NFIP, and thus, would be in conflict with prudent flood plain management. Also, administering S. 460 would create very serious problems in situations where there may be no clear evidence whether a building was in existence prior to the area's hazard identification date.

FEMA would be required to make an official finding as to whether the community's failure to participate was attributable to the insurance applicant and whether the applicant made a good faith effort to encourage participation. The need to make such a finding would be costly to the taxpayers and place an unmanageable administrative burden on FEMA.

Finally, the requirement that FEMA assure the eligible individual's compliance with normal flood plain management would in effect require FEMA to establish a national office on building standards in order to provide the necessary guidance for individuals in non-participating communities.

FEMA has also transmitted to the Congress a bill which would amend the insurance statutes to substitute the title "director, FEMA" for the title, "Secretary, HUD" wherever the latter appears and will also transmit statutory language giving Federal courts exclusive jurisdiction to hear and decide NFIP claims.

This concludes my prepared statement. I will be happy to respond to any questions the committee may have.

Mr. BRAGG. I could proceed directly to respond to some of the questions that Senator D'Amato raised earlier.

Senator HECHT. Well, since he's raised the questions, let's take his questions and then I have a lot of questions to ask you and Senator Hawkins I'm sure has, too. Since time is short, why don't you address Senator D'Amato's questions.

Mr. BRAGG. One of the questions that we face as we try to terminate the crime insurance program is that the flood insurance program is primarily focused in a few States and on that basis, why are we not recommending termination of the flood insurance program?

FLOOD AND CRIME INSURANCE PROGRAMS

Senator D'AMATO. Given the fact that the crime insurance program costs $20 million and we make a great big hullabaloo about subsidizing it, and the flood insurance program, which I again support, costs $1.5 billion.

Mr. BRAGG. Yes, Senator, I understand the question. There are several facts that distinguish the two programs.

First of all, the flood insurance program was designed to be an alternative to disaster assistance so that the moneys used to pay claims and expenses of the flood insurance program are those that would otherwise be required to be paid out in the form of disaster assistance. The flood insurance program provides an alternative which the crime insurance program does not.

In addition, there are nearly 2 million insured in the flood insurance program and less than 60,000 in the crime program. The flood insurance program is in all 50 States. The crime insurance program is only in 27 States and 3 territories.

The flood insurance program is not competing with the private sector because currently no private company is providing the type of flood insurance protection that we are providing. Potentially, there are 8 million insured that live in the flood plains who could

purchase flood insurance. We do not know the number of potential crime insurance participants, but there is a private market to handle these insureds.

Also, the flood insurance program can be self-supporting by 1988 if we're able to expand the policyholder base as we plan to do and continue our program of modest rate increases.

Additionally, we're working with the private industry, to involve them in the program, and through a phased-in basis, begin to have them take on more and more of the administrative chores of the national flood insurance program.

We think all of these reasons distinguish the two programs.

Senator D'AMATO. I haven't heard any yet. What about the problem of the small businessman who's in the ghetto area who cannot get any insurance? How do we deal with him?

Mr. BRAGG. Well, I think that there are alternatives and in fact many States——

Senator D'AMATO. The alternative is he closes down. He doesn't go into business. Do you know of any carriers who are going to take them in these high risk areas at rates they can afford?

Mr. BRAGG. Yes, Senator, there are alternatives to the Federal crime insurance program.

Senator D'AMATO. What are they?

Mr. BRAGG. Many States have adopted programs of their own. For example, the States of Michigan and New Jersey have separate crime insurance programs very similar to the Federal crime insurance program. Indiana and Wisconsin have less formal crime insurance programs where the commissioner places people with the private market who are having trouble finding coverage. Crime insurance is available through the FAIR plans in the States of Massachusetts, Rhode Island, Wisconsin, Michigan, Maryland, and Illinois. There are alternatives that can be adopted at the State level.

Additionally, there is crime insurance available in all 50 States through the private market.

Senator D'AMATO. So you're trying to make the State pay? That's what you're saying.

Mr. BRAGG. I'm saying for those States that have a problem—and not all States do—there is a viable alternative which many States have already adopted.

Senator D'AMATO. I can see that Mr. Stockman has gotten to you.

Let me ask you this. Haven't we reduced the loss ratios rather dramatically in the past 2 years?

RATE INCREASES

Mr. BRAGG. Yes, as a result of the improvements we've made in the program, including rate increases, we have reduced the loss ratio.

Senator D'AMATO. Who gave you the legislative authority to raise those rates? Wasn't it this committee? Didn't the Congress pass legislation that allowed you to raise rates?

Mr. BRAGG. As part of the original statute, yes.

Senator D'AMATO. OK. Let's stop beating our chests a little bit.

Mr. BRAGG. The point is that the rates were never raised in the history of the program until this administration.

Senator D'AMATO. I understand. So we allowed—Congress said we could keep the plan, but let's allow you to raise the rates; isn't that true?

Mr. BRAGG. The language that you put into the housing bill last year, sir, was never adopted. The rates were raised prior to the language that you put into the housing bill.

Senator D'AMATO. What is your intent in terms of dealing with the rates in the future? Is that one of the ways you can eliminate the program, make the rates so prohibitive? Is that your intention?

Mr. BRAGG. No, sir. We're still subsidizing the program at two to one. I don't think we've raised the rates to the point where the program is going to be eliminated.

Senator D'AMATO. You have a loss ratio for the year 1982. Don't you compute them on a monthly basis?

Mr. BRAGG. Yes, we do.

Senator D'AMATO. Have they indicated that those loss ratios are continually going down?

Mr. BRAGG. We're at about 1.75 loss ratio this year.

Senator D'AMATO. What were you last year?

Mr. BRAGG. 1.97.

Senator D'AMATO. So your rate is continually coming down. Can you go back to this committee over a period of time—can you give me the last year in progression?

Mr. BRAGG. Certainly.

Senator D'AMATO. Would you do that?

Mr. BRAGG. Certainly.

Senator D'AMATO. Do you have them here?

Mr. BRAGG. I would have to provide it for the record, sir. We didn't bring it with us.

Senator D'AMATO. Well, you've got this expert next to you.

Mr. BRAGG. The expert next to me has the loss ratio by year.

Senator D'AMATO. Would I be incorrect in stating that the ratios have been coming down for the last years?

LOSS RATIO DECLINING

Mr. BRAGG. From a loss ratio of 300 percent when we inherited the program, it has declined to the point where it should be 1.75 for 1983. I can bring you a chart that shows the month-by-month loss ratio.

[Information supplied for the record follows:]

FEDERAL CRIME INSURANCE PROGRAM
Loss Ratio by Month - October 1981 - Present

$ In Thousands

Month	Earned Premium	Expenses Incurred*	Loss Ratio
October	$1,091	$2,813	2.58
November	1,047	3,913	3.74
December	1,095	4,663	4.26
January	1,088	3,202	2.94
February	1,072	2,510	2.34
March	1,127	2,550	2.26
April	1,048	3,533	3.37
May	1,044	2,253	2.16
June	1,100	2,585	2.35
July	1,115	2,437	2.19
August	1,113	2,554	2.29
September	1,104	2,085	1.89
Total FY 82	13,038	35,098	2.69
October	1,115	2,191	1.97
November	1,054	2,049	1.94
December	1,113	2,667	2.40
January	1,333	2,205	1.65
February	977	1,671	1.71
March	1,162	2,476	2.13

*Includes all expenses except FIA administrative and interest expenses.

Senator D'AMATO. That's good. Don't be so uptight about it. Are you agitated because I take exception with your saying that even if the Congress—didn't you write these comments that the FIA chief aims for the crime insurance program—where you talk about how even if the Congress won't eliminate these programs, there are administrative ways which you can use to eliminate the crime insurance program? Are those your sentiments? In other words, if Congress wants to keep it, you're going to find a way to eliminate it? Is that what you meant?

Mr. BRAGG. No, sir.

Senator D'AMATO. Would you tell me what you did mean?

Mr. BRAGG. I meant that one of the reasons that we want to terminate the crime insurance program is that it is not cost effective. While we have made substantial improvements in reducing the loss ratio, I have not been successful with the Congress in trying to get them to eliminate the program.

With respect to the riot reinsurance program, I have been working with the private insurance industry matching reinsurance carriers with private sector insurance companies and persuading them to purchase their coverage through the private voluntary market. That program has been successful.

Senator D'AMATO. Mr. Chairman, I'd like to thank you for your patience and giving me the opportunity to go into this. As you know, I do feel very strongly about this particularly in light of the absolute necessity of this program. I just have one final question.

Do you think that there should not be programs that the Federal Government does not subsidize? Are you taking issue with the philosophy that there may be needs at times for the Federal Government to provide some form of subsidy?

Mr. BRAGG. My own philosophy is that if a program is not national in scope and there is an alternative to handling it federally, the program should be handled on a non-Federal level.

Senator D'AMATO. What efforts have you undertaken to inform the public, if any, of the existence of this program?

Mr. BRAGG. When we initially enter a State with the program, we meet with many insurance agents in the State and the commissioner. We tell them that if they are unable to find coverage through the private market, this program is available. If a potential insured contacts an agent and cannot get coverage, the agent would know he could provide it through the Federal crime insurance program.

My personal feeling is that the program was founded on the basis that the need for crime insurance was certified. That and the fact that the program is heavily subsidized would lead me to believe that we would not need to market the program aggressively. However, in the past, there was a marketing program nationwide and $450,000 was spent and it resulted in very little increase in the size of the policyholder base.

Finally, a GAO study quoted a 1980 letter from the superintendent of insurance from the State of California. He wrote that when California had their own crime insurance program, and this is a quote, "that after 8 years the California State crime insurance program there were 1,500 insured risks, although extensive advertising costs were incurred." He further stated that there was no evi-

dence that the subsidized policyholders could not have acquired insurance in the voluntary market or that such insurance would not have been affordable.

Senator D'AMATO. Didn't that same GAO study indicate quite clearly that the people in the eligible areas—as a matter of fact, two GAO audits indicated that the people in the areas of eligibility did not know about the program and had indicated that had they known of it they would have participated? So we can go round and round on that. Again, I point out to you when you talk about loss ratios, loss ratios have come down; yes, due to administrative improvement and, yes, due to the increase in rates, and I commend you for that. Whether we talk about 1,500 businesses or 30,000 businesses, many of those businesses will have no alternative and will be out of business. And I would suggest that when we become so doctrinaire in terms of the philosophy that we're going to give programs to the States and cut costs, that we create much more in the way of a $20 million loss to the Federal Treasury if those businesses or a substantial portion of them close down. It's going to be a loss of our taxpayers much, much more, not to mention the reduced quality of life in those communities.

So I just leave you with that thought.

Thank you, Mr. Chairman.

Senator HECHT. Thank you, Senator.

UNSUBSIDIZED RISK PREMIUM RATES ACTION BY FEMA

Mr. Bragg, what action has FEMA taken in the national flood insurance program to improve its process for setting the unsubsidized risk premium rates?

Mr. BRAGG. We have instituted a series of three rate increases in the national flood insurance program. They went into effect January 1, 1981, October 1, 1981, and June 1, 1982. Those rate increases programwide were 38 percent, 28 percent, and 20 percent. Again, those have resulted in significant savings to the Treasury.

The rate increases for 1981 generated $40.2 million for that year. The rate increases through fiscal year 1982 generated $68.2 million, and the increases through 1983 will generate $172.1 million.

Senator HECHT. When does FEMA expect these rates to cover their costs and be actuarially sound?

Mr. BRAGG. The goal is to do that by 1988.

Senator HECHT. Do the rates charged for insurance on new construction have to be adjusted from what might be an actuarial basis in order to compensate for the losses incurred by the subsidized programs for existing structures?

Mr. BRAGG. By statute, we have to subsidize existing construction. We have not reached a point in the program where the actuarially rated policyholders are subsidizing the nonactuarially rated. They are not subsidizing each other. There is still a deficit in the program.

Senator HECHT. Since you alluded to State Senator Jack Gannon's comments in your previous testimony, can you comment further on that since he's made the trip here?

Mr. BRAGG. Yes, and Dave McLoughlin will be testifying after me. He is in charge of our State flood plain management program and will elaborate on that.

There are a couple of assumptions made by the Senator that indicate we are not communicating with him properly. First of all, only those people who actually live in the flood plain would be regulated by flood plain management measures. The community must adopt flood plain management requirements. Those requirements would affect new construction within the flood plain so that there would be minimum standards placed on buildings put into the flood plain or the flood hazard area after the community entered the program. It would not affect existing construction and people who do not live in the flood hazard area would not be required to purchase flood insurance.

The flood insurance purchase requirements apply to people who live in the high hazard area and that is the only area that would be affected by new construction requirements.

Senator HECHT. On the riot and crime insurance, if Congress decides not to reauthorize the Federal crime insurance and riot reinsurance programs beyond the end of this fiscal year, what action will you and the Federal Insurance Administration take to assist those States that are currently participating in the programs?

Mr. BRAGG. We have begun that process already. We would have to meet with the superintendents of insurance of each of the states that had a problem, give them our statistical information, and provide information on how they could establish programs of their own if they cared to do so. We would work with the State legislatures in helping them to adopt legislation if that were necessary, and finally we would notify insureds and agents that the Federal program is no longer available.

Even if the program were terminated on September 30 of this year, there would be a runoff period of a year as the current policyholders began to phase out the program, so it would not be a situation where suddenly all 59,000 policyholders were without insurance. It would be a phase-out approach.

Senator HECHT. In the event these programs are not extended for another 2 years, could you restate for the benefit of the subcommittee what happens to those insureds who are currently under contract with the Federal Government?

Mr. BRAGG. All contracts would be honored for their duration.

Senator HECHT. All right. Later in the hearing we will receive testimony from the Superintendent of New York Insurance, Mr. James Corcoran—I don't know if he was able to make it here or not because the airport is fogged in. Have you read his testimony? He mentioned that one of the reasons for the high volume of policies in the State of New York is that the New York State Insurance Department actively publicized and marketed their existence. Your statement suggests otherwise. Would you explain this?

EFFECTS OF MARKETING SUBSIDIZED INSURANCE

Mr. BRAGG. Well, yes. I think there is room for disagreement on the effects of marketing. We had the earlier statement from the California Superintendent of Insurance who said it was not effec-

tive in his State. I would be willing to say that it is possible that if you aggressively marketed the program, you could sell policies. I'm not sure you would want to do that because, as you became more aggressive in your marketing strategy, you would potentially be taking insureds away from the private market because of the subsidized rates in the Federal crime insurance program. So I think it's clear that you could market anything that you cared to sell, but I'm not sure you want to do it with a subsidized program.

Senator HECHT. Thank you very much.

Senator Hawkins.

Senator HAWKINS. I have some questions, Mr. Chairman. I commend you for holding these hearings today. This program is of vital importance to my State, both parts. Six of the top eleven crime-plagued cities in the United States now have the honor of being in Florida. Also, the flood insurance is of vital importance to my State, especially this year. We are experiencing abnormally high water levels in every county.

I'm told you have improved the flood insurance program a lot. The insurance industry tells me there has been a great improvement in this program. Still a lot of people feel there's still room for more improvement. The insurance representatives that I spoke with and some other people that I've talked with said one of the continuing problems is the sending of endorsements where there are requests for changes in the policy.

Are you taking any steps to improve the program in that area?

Mr. BRAGG. Yes. The area that we hope holds the biggest promise for correcting those sorts of problems is our program simplification effort. For example, currently we have 69 different rating zones. We want to reduce that to six, which is much more consistent with the practices in the private insurance industry.

Senator HAWKINS. What would those six be?

Mr. BRAGG. They would be the "V" zone for coastral areas with wave action, but no elevations mapped; the V-zone with elevations; the high hazard areas of the "A" zone with elevations mapped; an unnumbered "A" zone, which includes insureds who live in a high hazard area that has not yet been mapped with elevations; combined "B" and "C" zones; and than "all other."

Senator HAWKINS. You mean there are areas that haven't been mapped at all?

Mr. BRAGG. Yes. There are some areas that have never had flood insurance rate maps.

Senator HAWKINS. Who's fault would that be? The local area or is this a national program?

Mr. BRAGG. We have 17,000 communities to map and we do as many each year as we are able to. It's a long process.

PAID SURVEYS REQUIRED

Senator HAWKINS. Do you still require a survey paid for by the homeowner before he can renew his policy annually?

Mr. BRAGG. Only in some cases. For example, if the homeowner would want special rating treatment or he wanted to certify that he was at a certain elevation in order to get a reduced rate, that's when we would require a certification.

Senator HAWKINS. I don't understand how, if you live on the water or on a lake which is very common in my State and you get flood insurance annually and then next year when you want to renew it they ask for a survey which costs about $200. Why doesn't the first survey handle it?

Mr. BRAGG. Certification is required for new construction. Owners of existing construction can certify their elevations in order to receive a lower rate.

Senator HAWKINS. Was that not true the first time they got insurance?

Mr. BRAGG. That's a good question.

Senator HAWKINS. Well, I think it's an undue burden on the homeowner who builds a house or buys a house and as his first insurance policy he gets homeowners and the insurance agent then tells him you live on the water and you have to get flood insurance. What do you do to get flood insurance? Well, you have a survey taken. We'll provide a survey. It cost $200 for a neighbor of mine and the next year came the notice, "Do you want to renew the flood insurance?" "Yes." "Well, you'll have to take another survey." Now this is making surveyors rich in Florida and it's making the homeowners very irritated. Very few people I know have flood insurance in this particular area that I'm talking about on lakes, and yet in addition to the policy you have to pay the surveyor.

Mr. BRAGG. We only require a survey for new construction or if we think there's a chance of lowering the person's rate. Additionally, in almost all cases they can provide the same information that a survey is required to do by going to their community and——

Senator HAWKINS. You can get it from the local city hall who has your original survey plat on file.

Mr. BRAGG. We accept that as the elevation.

Senator HAWKINS. Well, the insurance agents don't know it. Whose fault is that? That's another problem—the lack of instructions that the local agents receive from the Federal program. Is that lack of communication?

Mr. BRAGG. We will need to communicate further with the agents if they're having trouble understanding the instruction. It is our responsibility to do that. I have to confess that the surveys have not been coming in in great numbers.

Senator HAWKINS. That's a tremendous burden.

Mr. BRAGG. We have examined the process. The idea is to accurately reflect the risk.

Senator HAWKINS. When the house is built.

Mr. BRAGG. Yes, Senator.

Senator HAWKINS. I don't think it should alter yearly and go up and down. When you buy property in Florida they'll give you the 10-year average of the water table there. Water management is a big business in Florida and they'll tell you what the water table was on that body of water for the last 10 years. Then you survey it before you ever build a house on it. There are a lot of State laws you have to meet. When you get your insurance policy for your regular homeowners policy, then they say you live on the water and I suggest you get flood insurance. That's the first time most people hear about it. They come from landlocked cities to my State to

build a home and they do it and then when they go to renew it they hit the fan, and a lot of them drop it and they should not. I think one survey is adequate and should be adequate. That's a tremendous expense in my State to have to do it annually upon renewal and have an expiration date if you don't get the survey. It is an undue burden on the homeowner.

Mr. BRAGG. I agree and I think it's a problem of communication. We would not require two unless the person had made some changes which would cause him to be at a lower rate or a lower risk. There apparently is a problem of communication, and I will look into that.

Senator HAWKINS. Will you look into that and let me hear from you?

Mr. BRAGG. Yes.

Senator HAWKINS. There's also a perception that part of the problem is that your old contractor was an expert in the computer field and he didn't understand the insurance field. Do you feel there will be an improvement with your new contractor in light of his title that's called the Computer Sciences Corp?

Mr. BRAGG. We hope to have the most improvement in that area with our effort to involve the insurance industry in marketing the program and then channeling their information through our contractor. If we're successful in this effort, not only would the agents have better communication with their own companies whose staffs they work with continuously, but they will also be dealing with insurance people who process applications and claims every day as part of their daily business.

Senator HAWKINS. Was that not the fact with the old contractor? Didn't the old contractor, who was a computer specialist, work daily with the insurance people?

Mr. BRAGG. We were not involving the private insurance industry with the old contractor. Our program is to involve the industry in servicing the program. We have not implemented that yet. Once we do, and I hope to by October, that should solve some of the problems.

Senator HAWKINS. Is there some way you could have the computer specialist take the insurance course that's required in my State or your State or anyplace else like that? It's a basic. I know a lot of people who have taken an insurance course just to have it under their belt. It seems to me that the man that's going to be at the helm here ought to understand insurance.

Mr. BRAGG. I do.

Senator HAWKINS. I know, and I'd like you to help your new contractor named the Computer Science Corp. understand insurance.

Mr. BRAGG. The Computer Science Corp. has retained insurance experts to help them, but additionally we want to move to a program where we have computer people doing computer work and insurance people doing insurance work.

Senator HAWKINS. And who's going to punch it in?

Mr. BRAGG. The insurance people will be doing all of this themselves for companies who care to participate.

Senator HAWKINS. They'll fill out the forms and punch it and do all this and hand it to a computer.

Mr. BRAGG. Yes.

Senator HAWKINS. One last question, Mr. Chairman. I have some akin to Senator D'Amato's, but time is running by and I'll submit mine in writing if you would like and you can respond by writing to shorten the time.

You indicate in your testimony you want to make the flood insurance program self-supporting. I applaud that. If you'll tell me the nature of the natural disasters that we're going to have next year and if you feel that there's a limit we can go to in raising the premium and still retain a viable program.

Mr. BRAGG. Clearly there is a great deal of controversy over making a program like the flood insurance program self-supporting. My position is based on the experience we've had. We know that structures built in a special flood hazard area in compliance with community flood plain management ordinances have a 1 percent chance per year of being flooded. We know now that the average claim paid is about $6,000. This is experience we've never had before. We also know that many insurance companies are able to make money based solely on high risk coverage. They specialize in that kind of coverage.

While we may not get to a point where we will have sufficient reserves to pay for catastrophic losses, I think we will be able to get to a point where on the historical average year we will be able to generate enough premium income to meet the losses and expenses and in fact, for the first time, we did so last year. That was a result in a very large part of reduced flooding activity, but also as a result of the improvements we made.

Senator HAWKINS. I'm not going to spring anything on you but I am going to include sinkhole insurance in the program. It's not covered under FEMA. It's not covered under emergency. It's not covered under flood. It just swallows the houses and the small businesses. We have five businesses that were sucked in by the huge Winter Park sinkhole. They were too small. If they had been bigger businesses they would be covered. So I don't want to spring it on you, but I'm going to add it to the bill.

Thank you, Mr. Chairman.

Senator HECHT. Thank you, Senator.

I just want to ask you one last question and I have a few more questions that I'm going to ask you for the record later on.

FEMA'S RESPONSE TO SOUTH AND MIDWEST FLOODS

The news reports of the last few days have made us dramatically aware of the current flooding of the South and Midwest. One of our witnesses today, Ms. Beriwall from Baton Rouge, La., canceled her appearance today because of record flood levels in that State. In my own State of Nevada around the Reno area they have floods that are facing a potentially dangerous situation because of the large amount of precipitation over the winter which in the event of an early thaw in the high country could cause a severe hardship.

Could you explain to the subcommittee exactly what you and the FEMA are doing at this time for the current situation in the South and Midwest and what action do you take for the potential risk that exist for Reno, Nev?

Mr. BRAGG. Currently the Corps of Engineers is in the South, in the Louisiana area trying to mitigate the damages being caused now by the floods. As an agency, of course, we will respond if a disaster declaration is made for that State. As the insurance administrator, I will have staff in Louisiana as soon as the weather clears and set up an onsite claims office as soon as possible to help insureds get immediate settlement on their claims. In cases like this, we make on-the-spot claims payments, at least partial payments, to help people have some money to be able to respond to the emergency.

With respect to your own State, we monitor the weather every 3 or 4 hours to gain knowledge and determine what action will be required in case we need to send a team to set up these onsite claims offices.

Senator HECHT. Thank you very much. We appreciate your appearance.

Could we have the next panel, please? Mr. McLoughlin, can you kind of summarize in 5 minutes?

STATEMENT OF DAVID McLOUGHLIN, DEPUTY DIRECTOR, STATE AND LOCAL PROGRAMS SUPPORT, FEDERAL EMERGENCY MANAGEMENT AGENCY

[The complete statement follows:]

Senate Oversight Hearings
Committee on Banking, Housing and Urban Affairs
Subcommittee on Insurance
Testimony of Dave McLoughlin, Deputy Associate Director,
State and Local Programs and Support, FEMA

I am pleased to appear before this Committee on behalf of the Federal Emergency Management Agency (FEMA), to discuss the major floodplain management accomplishments of the National Flood Insurance Program (NFIP). A copy of my testimony is provided for inclusion in the record of this hearing.

Mr. Bragg has addressed the importance of the insurance aspects of the NFIP. Therefore, I would like to discuss the major accomplishments, the future direction and the needs of the NFIP in meeting the floodplain management and flood insurance studies objectives.

FLOOD STUDY EFFORT

As Mr. Bragg has indicated, most communities now have some degree of flood insurance protection. Nevertheless, reduction of future losses depends upon the ability of the States and local communities, and the individual property owners, to utilize the flood data provided in FEMA's flood insurance studies in order to implement the measures needed to protect themselves against future damage, and to protect the Nation against the continuing high cost of disaster assistance.

The NFIP Act of 1968 stated that flood risk zones should be established for all the flood-prone areas within 15 years, a period which expires this August. We have submitted proposed legislation for Congressional consideration that would extend this time limit to September 30, 1987. There are two basic reasons why this extension is necessary. First, in 1968, the number of flood-prone communities to be studied was estimated at 5,000, a number which has more than tripled while no extension of the time limit has been granted for their completion. Second, in spite of actions taken to reduce study costs, budget and staff allocations have not been sufficient to complete the assignment.

FEMA designates as flood insurance studies (FIS) those studies used to determine flood risk zones. The FIS are used to convert communities from the emergency phase to the regular phase of the NFIP. The FIS provide the basic information needed for flood hazard area identification and risk assessment. The FIS provide data used as a basis for construction techniques to reduce flood damage and for making prudent development decisions. These risk studies provide the tools both for implementing sound floodplain management and for setting actuarial insurance rates. Each of the States, more than 50 Federal agencies, and countless numbers of developers, property owners, and businesses utilize the NFIP data base and floodplain management standards in planning actions involving the Nation's floodplains.

The following are examples where extensive use is made of FIS data by other Federal agencies. The National Weather Service uses the data to assist in flood prediction and warning. The Department of Transportation uses the data in the design of stream crossings. The Environmental Protection Agency uses the data in the design of water and sewer systems.

Let me briefly outline the magnitude of the NFIP assignment. There are more than 19,000 communities in the Nation which we have identified as flood prone. Of these, flood risk studies are completed or underway for some 10,000 communities. An additional 2,000 have been determined to be minimally flood-prone and have been converted to the regular phase of the NFIP. Approximately 7,000 communities remain to be evaluated in order to determine whether a flood risk study is currently needed or will be needed in the future.

In FY 82, 1,060 flood insurance studies were completed and 77 new studies, 29 restudies, and 158 studies utilizing existing data were initiated. There were 1083 communities converted from the emergency phase to the regular phase of the NFIP which means that these communities have flood elevation data that provides the minimum levels for elevating and floodproofing structures and for the setting of actuarial rates.

In FY 83, we plan to convert an additional 1,500 communities from the emergency phase into the regular program, bringing the total number of communities in the regular program to more than 10,250. Our study program will entail completing 957 flood insurance studies, and initiating 165 new studies, 72 restudies, and 85 existing data studies. FY 83 funds will also be used to produce flood insurance maps on designated undeveloped coastal barriers to reflect the non-availability of Federal flood insurance after October 1, 1983.

As I indicated earlier, approximately 7,000 more communities need to be evaluated to determine the exact number, priority, and level of analyses needed. Many of the remaining communities are small, with low population density, and unlikely to experience significant development in the next 10-15 years. An evaluation effort to be completed this fall will determine which communities will require a detailed flood insurance study and which can be converted to the Regular Program without a study. Whenever adequate flood elevation data are available from Federal, State or other floodplain studies, this existing data will be used to develop a flood risk map for community conversion to the regular program. The results of this evaluation will be used to refine our four-year plan for completing the flood insurance studies for unstudied communities.

In summary, since the FIS program began in 1968, $606 million have been spent to: (1) provide Flood Hazard Boundary Maps for more than 19,000 communities, (2) initiate and process Flood Risk Studies for more than 10,000 communities, and (3) complete minimal conversion studies for 2,000 communities. To complete

the FIS program, it is roughly estimated that, within the next four years, a maximum of 3000 communities will require flood risk studies averaging $50,000 per community or a total of $150 million. Communities not designated for study will be placed in the Regular program through the minimal conversion process.

FLOODPLAIN MANAGEMENT

As FEMA works toward effecting a reduction in flood losses through floodplain management, we are addressing the delineation and mitigation of other special flood hazard problems such as mudslides and alluvial fan areas and urban drainage issues. We are also addressing floodplain use problems through special studies such as those for water-dependent port activities and Appalachian communities exemplified by Harlan County, Kentucky which because of their unique circumstances need to be looked at differently to assure achievement of floodplain management goals. An advance notice of proposed rulemaking has generated over 400 comments suggesting ways of improving the regulations. These efforts will provide input to FEMA's review and proposed update of its revised floodplain management regulations scheduled for publication this fall.

In carrying out its flood hazard mitigation responsibilities, FEMA has increased its efforts toward providing technical assistance to Federal, State and local officials; private industry; and individual property owners. Examples of

technical assistance provided include: (1) developing a design manual for floodproofing of nonresidential structures; (2) assisting Lycoming County, Pennsylvania, in developing a prototype flood warning system; and (3) developing workshops to train architects, engineers, builders and local officials in techniques of constructing residences in coastal areas.

Assistance also is provided through the State Assistance Program (SAP), the Hazard Mitigation Teams, and acquisition of property under Section 1362, P.L. 90-498. Through the SAP and with the assistance of our NFIP State Coordinators and the Association of State Floodplain Managers, State capabilities have been strengthened and expanded significantly during recent years. During the recovery period immediately following disasters, Hazard Mitigation Teams led by FEMA, but composed of other Federal agencies provide assistance to States and local communities in strengthening their efforts against future losses. Since the inception of this type of assistance in 1981, some 25 teams have been assembled to collect information and recommend long run flood loss reduction measures.

FEMA continues to work with National Building Code organizations and related building interest groups to develop strategies for improving flood resistant design and construction of buildings. Recent integration of the NFIP standards into the Southern Standard Building Code (SBCC), and the proposed integration by the Building Officials and Code Administrators Code (BOCA) are important steps to strengthen floodplain management.

There has been considerable discussion regarding community enforcement of NFIP floodplain management standards adopted into local ordinances. A recent General Accounting Office report focused on FEMA's conduct of Community Assistance and Program Evaluation meetings, referred to as CAPEs. In response to the findings contained in this report, and FEMA's own evaluations, FEMA has re-examined its procedures for monitoring community performance as well as overall program effectiveness.

Recent initiatives that address these deficiencies include the funding of selected States to conduct CAPE meetings and a pilot program to assess the feasibility of Corps of Engineers participation.

FEMA has enhanced its capabilities for accessing and analyzing, computerized data from various sources such as flood insurance policies and claims. These improved capabilities will allow FEMA to focus its monitoring activities on those communities in which the most intense development is occurring or in which enforcement problems may be evident. FEMA also will be better able to assess the overall effectiveness of floodplain management throughout the Nation as a whole and to evaluate community program performance standards.

Preliminary analysis of available data indicates that, despite problems with individual communities, the overall program is working as intended. Information obtained from the elevation certificates that accompany each flood insurance policy indicates that 97 percent of all new, insured construction built in

communities for which flood studies have been conducted is at or above the 100 year, or base flood, elevation. FEMA believes that the data reasonably reflect floodplain development in general. The combination of local floodplain management regulations and the application of actuarial flood insurance rates appears to have resulted in a significant improvement in the safety of floodplain construction.

FEMA recently has been assigned an important new role in floodplain management leadership. In September 1982, the Office of Management and Budget assigned to FEMA responsibility for the Unified National Program for Floodplain Management. An important aspect of this program is its interagency floodplain management task force consisting of Federal agencies with water resource interests. Previously, this responsibility had been assigned to the Water Resources Council. The Congress authorized the Unified Program in Section 1302(c) of the NFIP Act of 1968.

On March 29, the General Accounting Office (GAO) discussed with FEMA the findings from its study of flood insurance studies and the emergency program. Three action options were discussed: (1) allow the emergency program to lapse; (2) extend the emergency program until the flood insurance study program has been completed in 1987, as recommended in the Administration's budget; and (3) convert all emergency program communities to the regular program by August 1983 using existing flood hazard boundary maps and where necessary initiating flood insurance studies after the conversion. At this time? FEMA believes the second option is the perferable course of action. This option provides for orderly completion of studies necessary to ascertain flood risk. It allows for use of

the evaluation we are undertaking to identify communities likely to experience future development. It maintains the government's commitment to provide a limited amount of insurance until a detailed evaluation of flood risk has been completed and until a community has accepted responsibility to manage future floodplain development through the adoption and enforcement of ordinances designed to reduce future flood losses.

In conclusion, I wish to restate several points:

(1) The NFIP explicitly establishes the interdependence of flood insurance and floodplain management.

(2) The objective of floodplain management is to reduce future flood losses.

(3) Hazard identification and risk assessment through a flood insurance study is the foundation of floodplain management.

(4) Finally, to assure implementation of successful floodplain management at the local level, there must be an orderly conversion of communities from the Emergency Phase to the Regular Phase of the Program.

This concludes my prepared testimony, I will be happy to answer any questions you may have.

Senator HECHT. Thank you very much.
We will now hear from Mr. Dodge.

STATEMENT OF LOWELL DODGE, ASSOCIATE DIRECTOR, RESOURCES, COMMUNITY AND ECONOMIC DEVELOPMENT, GENERAL ACCOUNTING OFFICE; ACCOMPANIED BY JAMES NOEL AND JOHN NICHOLSON

Mr. DODGE. I'd like to introduce, if I may, Mr. Chairman, my two colleagues, James Noel and John Nicholson, who played a major part in our study of this area.
[The complete statement follows:]

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Statement of Lowell Dodge

Associate Director

Resources, Community and Economic

Development Division

Before the

Subcommittee on Insurance

Committee on Banking, Housing, and Urban Affairs

United States Senate

on

Alternative Approaches for Converting

Communities in the National Flood Insurance Program

from the Emergency Phase to the Regular Phase

Mr. Chairman and Members of the Subcommittee

We welcome your invitation to discuss our ongoing review of the Federal Emergency Management Agency's (FEMA's) progress in converting flood-prone communities from the emergency phase to the regular phase of the National Flood Insurance Program. I will highlight the tentative findings of our review and present options we believe the Congress could consider in

connection with the expiration of the emergency phase of the program in May 1983. I will also briefly summarize the findings in our January 3, 1983, report entitled "National Flood Insurance Program--Major Changes Needed If It Is To Operate Without A Federal Subsidy." This report reviewed how FEMA sets the rates policyholders pay for flood insurance and how flood insurance is financed.

In summary, Mr. Chairman, we have found that FEMA will not meet the August 1983 deadline contained in the National Flood Insurance Act of 1968 for providing flood insurance rate maps for all the Nation's flood-prone communities. FEMA was expected to map over 17,000 communities in the last 15 years. Our tentative findings indicate that faced with this task, FEMA relied primarily on a technique for producing rate maps which was both costly and time consuming. FEMA did not make as much use as it might have of alternative approaches. Without any action by the Congress, about 291,000 policyholders will soon lose their flood insurance coverage. To avoid this result, we believe the Congress needs to consider and select an optional approach to complete the mapping project.

THE NATIONAL FLOOD INSURANCE PROGRAM--ITS OBJECTIVE AND OPERATION

Before the establishment of the National Flood Insurance Program, flood victims turned to Federal and State governments for most of their relief and rehabilitation needs. To stem the growing demand for Federal disaster assistance, the Congress passed the National Flood Insurance Act of 1968. Under the provisions of the 1968 act, as amended, property owners in flood-prone areas are eligible to purchase flood insurance but only if their community, such as a city or county, joins the program and adopts and enforces adequate flood plain management

regulations designed to protect lives and property from future floods.

Under the original approach for determining what insurance rates would be charged in a community, a flood insurance rate map, which shows the various zones of flood risk, had to be prepared. Once the rate map was completed, a community could enter the program. The rates a policyholder paid for flood insurance depended on which risk zone he was in as shown on the rate map. Policyholders in zones which border a river or coastline generally face a greater risk, and thus are charged higher rates.

Because of start-up problems and the need to collect detailed engineering data in each community, preparing these rate maps proved to be time consuming and inhibited communities' ability to join. In fact, in the program's first year of operation, only four communities joined and only a handful of insurance policies were sold.

To allow easier entry into the program, the Congress, in December 1969, amended the 1968 act to create an "emergency" phase. This phase permitted a community to be admitted without a flood insurance rate map. Instead, a flood hazard boundary map--a less detailed map which broadly identified a community's flood-prone areas--was used to admit a community to the emergency phase. As with the "regular" phase, FEMA requires an emergency phase community to adopt flood plain management regulations to guide new construction in flood-prone areas. These regulations are less stringent in the emergency phase than those in the regular phase reflecting the reduced level of detail in the flood hazard boundary map. In addition, because the flood hazard boundary maps identify only broad areas of

risk, a flat insurance rate is charged all policyholders regardless of how they are situated relative to the source of flooding.

FEMA WILL NOT MEET THE 1983 DEADLINE--
THOUSANDS OF COMMUNITIES REMAIN
IN THE EMERGENCY PHASE

The emergency phase is a temporary aspect of the program that is reauthorized periodically and is currently set to expire in May 1983. The emergency phase was expected to expire eventually because FEMA was to have completed, by August 1983, the development of the flood insurance rate maps used to convert communities to the regular phase of the program. FEMA will not meet the August deadline for developing flood insurance rate maps for all the Nation's communities. Currently, about 17,300 communities are participating in the National Flood Insurance Program; however, only about 8,600 are in the regular phase of the program, while about 8,700 remain in the emergency phase. FEMA is in the process of mapping about 1,400 emergency phase communities. This leaves almost 7,300 emergency phase communities still in need of a flood insurance rate map in order to be converted to the regular phase.

Given that the 1968 act provided 15 years for developing the rate maps and that over $606 million has been appropriated for mapping, the question arises: What has prevented FEMA from developing flood insurance rate maps for all the Nation's flood-prone communities? Our review has suggested several factors.

An initial factor was the unexpected magnitude of the undertaking. When the 1968 act was passed, it was estimated that there were about 5,000 flood-prone communities in the Nation. However, as the process of identifying flood-prone

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communities proceeded, the total proved to be over 20,000, or four times the original estimate. Eighty-seven percent of those communities elected to join the program.

Our audit work to date indicates that FEMA, faced with developing flood insurance rate maps for over three times the number of communities in the original estimate, did not consistently use available alternative techniques for producing rate maps which were less costly and less time consuming.

There are three basic techniques for producing a rate map. The first is to develop hydrologic and engineering data and create a detailed rate map, showing, for example, the height of flood waters during a 100-year flood and the various flood risk zones. This mapping technique can provide useful information for large, developing areas to use in setting and enforcing flood plain management regulations designed to prevent future flood losses. This process has cost, on the average, about $50,000 per community and usually takes about 4 years.

A second technique is to produce a rate map using available existing data on a community's flood experience and its potential for future flooding. This technique does produce a less detailed map than the first approach, but FEMA has estimated that this technique can cost significantly less, about $8,000, and usually takes about 2 years.

A third technique is to simply convert the less detailed flood hazard boundary map, which is used to admit the community to the emergency phase, into a rate map. This last approach can be used in areas where flood plain management information is judged to be less critical, can cost as little as $1,000, and usually takes less than 2 years.

FEMA has relied on the detailed map technique for most of the program's life. Between 1968 and 1972, FEMA developed the

methods for producing rate maps using the detailed map technique. For the next 5 years it produced primarily detailed rate maps.

Beginning in 1977, FEMA began to explore using the less costly alternative mapping techniques. In March 1979, we issued a letter report to the Secretary of Housing and Urban Development that expressed concern about whether FEMA would meet the 1983 deadline. FEMA responded by placing more emphasis on alternative mapping techniques. FEMA used these techniques to produce rate maps for several hundred communities. However, FEMA officials, in March 1981, adopted the view that the alternative techniques were no longer advisable and the emphasis returned to the detailed study technique.

Recently, FEMA proposed in its fiscal year 1984 budget to once again make use of alternative techniques for producing rate maps. However, the net result has been that since 1968, in the three FEMA regions we visited, about 82 percent of almost 4,200 regular phase communities were converted using the more expensive and time consuming detailed mapping technique.

OPTIONS ARE AVAILABLE TO THE CONGRESS REGARDING THE REMAINING EMERGENCY PHASE COMMUNITIES

Allowing the current emergency phase to lapse without taking any further action, in our view, is simply not a desirable course of action. After their policies expire, about 291,000 policyholders living in communities now in the emergency phase would be without flood insurance. Further, about 8,700 communities would no longer have the incentive Federal flood insurance provides to enforce even the minimal flood plain management regulations required in the emergency phase. Without the availability of insurance and the enforcement of flood plain management regulations designed to reduce future flood losses,

the demand for Federal disaster assistance could increase, contrary to a basic objective of the National Flood Insurance Act.

As an alternative, FEMA has proposed to the Congress extending the mapping deadline and reauthorizing the emergency phase of the program until September 1987. The obvious benefit of this option is that flood insurance and flood plain management regulations would continue in force for the 8,700 emergency phase communities. However, without any substantive changes in how FEMA performs the mapping function, this could be a costly, time consuming alternative.

FEMA has estimated that it would take about $153 million in current dollars to complete the mapping effort. This estimate, to FEMA's credit, assumes reduced reliance on detailed mapping and increased emphasis on the less costly alternative techniques. Our review, however, suggests that FEMA's estimate may understate the total cost. The estimate assumes that the cost of a detailed map will be $50,000. However, for fiscal year 1983, the cost of a detailed map will average around $88,000. If future costs reflect 1983 averages, instead of FEMA's current estimate, the total mapping cost could run much higher.

Even with less reliance on detailed mapping, FEMA is still proposing to convert almost 3,000 communities with the detailed maps that take about 4 years to complete. Consequently, we believe it is unlikely that the effort will be completed by FEMA's proposed 1987 expiration date. We believe that it will probably take more time--possibly an additional 5 years. In our discussions with FEMA officials they also agreed that the effort could extend well beyond 1987.

If the mapping effort is extended, we believe that the Congress, either through legislation or committee report, could require FEMA to review each community and select the optimum conversion method which balances the extra information obtained by detailed mapping against the need for that information when less costly alternatives are available. This action is important because we found that FEMA has not set any priorities for its mapping effort, allowing its various regions to select communities for mapping based on widely different criteria. This resulted in some undeveloped, relatively less flood-prone communities receiving rate maps, while other more flood-prone areas remained in the emergency program. In addition, based on our review, we believe that very few of the 7,300 communities still in need of rate maps will require a detailed map. By reviewing each community and selecting the optimum conversion method, FEMA will be able to develop concrete information for the Congress on how long the mapping will take and how much it will cost.

Another option is to convert the remaining emergency phase communities into the regular phase using the less detailed flood hazard boundary maps. To avoid a prolonged conversion program the Congress could amend the 1968 act to require FEMA, before the August 1983 mapping deadline, to use the flood hazard boundary maps as a basis for establishing insurance rates for emergency phase communities. FEMA has already used boundary maps to produce acceptable rate maps in less developed areas typical of those remaining in the emergency phase. This option would be considerably less expensive than the option of continued mapping since it would involve primarily the administrative cost of informing the communities of the change. It could also be accomplished quickly.

A drawback of this option is that the extra flood plain management information which the detailed maps provide, such as the height of flood waters during a 100-year flood, would not be available. This information is used to establish and enforce flood plain management regulations and, based on our review, appears to be critical only where an area is developing or is likely to develop. Our limited review of communities remaining in the emergency phase indicates that they are largely areas that have few insurance policies--96 percent of them have less than 100 insurance policies in force--and are unlikely to see significant development. Therefore, we believe that the additional information a detailed map can supply may not be worth the cost for the vast majority of the 7,300 communities still needing rate maps. In any event, the act could be amended to make clear that FEMA can perform detailed mapping where it is necessary to collect additional data to identify detailed flood risk zones. However, similar to our proposal for the first option, we believe the Congress needs to require FEMA to make a positive determination on which areas need detailed rate maps before proceeding with the maps. In this situation, a detailed map would be an exception to the rule of converting using the flood hazard boundary map. We are prepared to assist the subcommittee in developing the necessary amendments to implement this option.

OTHER IMPROVEMENTS CAN BE MADE TO THE FLOOD INSURANCE PROGRAM

Over the last several years we have issued numerous reports suggesting improvements in the flood insurance program. Our January 3, 1983, report entitled "National Flood Insurance Program--Major Changes Needed If It Is To Operate Without A Federal Subsidy" reviewed how FEMA sets rates for flood

insurance and how the program is financed. Appendix I of my statement contains a complete list of our reports on the flood insurance program.

The program has two rate classes. Unsubsidized rates are charged policyholders insuring new structures built after the flood insurance rate map is put into effect. Subsidized rates are charged policyholders insuring existing buildings built before the flood insurance rate map.

We found that because of data and methodological weaknesses, the program's unsubsidized rates had not generated enough premium income to cover associated claims and operating costs and were, in fact, being subsidized by the Federal Government. Between 1978 and 1981, the aggregate deficit per policy ranged from about $20 to almost $200. We also found that despite three rate increases since January 1981, the rates were still inadequate. We noted that FEMA was aware of these weaknesses and had taken some action to improve its ratesetting process. Nevertheless, we made a series of recommendations to the Director, FEMA, to improve the ratesetting process so that the unsubsidized rates would produce adequate premium income as required by the act, as amended.

Regarding the intentionally subsidized rates, we reviewed alternatives for eliminating the Federal subsidy these rates contain. We did this because FEMA has proposed terminating the program's Federal subsidy by 1988. The alternatives we identified included increasing the intentionally subsidized rates, reducing the amount of coverage, cross-subsidizing with a surcharge on unsubsidized ratepayers, or a combination of these options. We noted that such actions could cause some policyholders to drop their flood insurance policies and increase their reliance on Federal disaster relief in the event

of a flood, contrary to the program's objectives. We recommended that FEMA establish a monitoring program to detect any adverse impacts which increases in intentionally subsidized rates or decreases in coverage provided at the intentionally subsidized rates could have on the flood insurance program's objectives. FEMA has begun collecting data to perform such monitoring.

We also noted that FEMA's proposal to eliminate the Federal subsidy was a pronounced departure from how the program had been administered since 1968. Consequently, we suggested that the Congress itself might wish to address the question of whether it wants the subsidy eliminated and, if so, how the elimination should be accomplished.

To finance flood insurance, the Congress established a revolving fund and gave FEMA $1 billion in borrowing authority. Such funds are typically used to finance Government programs which are business-like in their operation.

Our views on the use of revolving funds have been governed by our concern about the Congress weakening its control over program activities when it authorizes this funding mechanism. Consequently, it has been our view that revolving funds may be appropriate when (1) a continuing cycle of operations generates receipts, principally from the public, (2) a substantial need exists for flexibility, and (3) the fund is or likely will be self-sustaining.

Because premium income did not cover costs, the Agency financed the insurance program's losses by borrowing funds from the Treasury. Between 1970 and 1980 it borrowed about $854 million and by the start of fiscal year 1981 had almost exhausted its borrowing authority. Appropriations in fiscal

years 1981, 1982, and 1983 repaid this borrowing and in the process restored FEMA's borrowing authority to just under $1 billion.

Although it borrowed money each year, FEMA was not required by its enabling legislation to regularly request appropriations to repay its borrowings. We believe that the lack of a regular requirement to request appropriations to repay borrowings has reduced the ability of the Congress to oversee the flood insurance program and to identify why the program has been operating at a deficit. We offered the Congress two options to increase its control over the program's financing. These options were to (1) retain the revolving fund but amend the 1968 act to give the Congress greater control over how FEMA finances its losses or (2) amend the 1968 act to eliminate the revolving fund and finance the program through direct appropriations. We believe retaining the revolving fund is appropriate if the subsidy will be eliminated within the foreseeable future. If, on the other hand, the subsidy will remain a long-term feature of the program, we believe a direct appropriation would be a preferred approach. The amendments necessary to implement either of these options are in appendix II of my statement.

Mr. Chairman, that concludes my prepared statement. I would be happy to answer any questions the subcommittee might have. Thank you.

APPENDIX I

GAO REPORTS ON THE
NATIONAL FLOOD INSURANCE PROGRAM

Report Title	Issue Date	Reference Number
Actions Needed to Provide Greater Insurance Protection to Flood Communities - Federal Insurance Administration	7-19-73	B-178737
National Attempts to Reduce Losses from Floods by Planning for and Controlling the Uses of Flood-Prone Lands - Multiagency	3-7-75	RED-75-327
Tulsa, Oklahoma's Participation in the National Flood Insurance Program - Federal Insurance Adm.	9-19-75	RED-76-23
Formidable Administrative Challenge Achieving Natonal Flood Insurance Program Objectives	4-22-76	CED-76-94
Report to HUD Secretary: Financial Controls Over National Flood Insurance Program	3-21-77	CED-71-47
Report to Senator Eagleton: The Johnstown Area Flood of 1977: Case Study for the Future	5-5-78	CED-78-114
Report to Senator Eagleton: FIA's Conversion of National Flood Insurance Program from Industry-Operated to Government-Operated	5-31-78	CED-78-122
Report to HUD Secretary: Efforts to Reduce Flood Losses: FIA's Flood Insurance Program	3-22-79	CED-79-58
Examination of Financial Statements of the National Flood Insurance Program as of December 31, 1977	6-1-79	CED-79-70
How Do Federal Agencies Assure That Disaster Loan Recipients Maintain Mandatory Flood Insurance?	6-1-79	CED-80-10
Report to Senators Garn and Metzenbaum: Termination of the Map Information Facility Contract by FEMA	5-12-81	CED-81-99

APPENDIX I

Report Title	Issue Date	Reference Number
Terminating the Audit of the National Flood Insurance Program's Fiscal 1980 Financial Statements	9-21-81	AFMD-81-93
Claims processing procedures of the National Flood Insurance Program	3-5-82 5-19-82	AFMD-82-56
Follow-up on claims processing procedures of the National Flood Insurance Program	7-22-82	GAO/AFMD-82-56S
National Flood Insurance: --Marginal Impact on Flood Plain Development --Administrative Improvements Needed	8-16-82	GAO/CED-82-105
National Flood Insurance Program--Major Changes Needed If It Is To Operate Without A Federal Subsidy	1-3-83	GAO/RCED-83-53
The Effect of Premium Increases on Achieving the National Flood Insurance Program's Objectives	2-28-83	GAO/RCED-83-107

APPENDIX II

PROPOSED AMENDMENTS TO THE

NATIONAL FLOOD INSURANCE ACT OF 1968

TO INCREASE CONGRESSIONAL OVERSIGHT AND CONTROL OF THE

NATIONAL FLOOD INSURANCE FUND

Section 1: This act may be cited as the "National Flood Insurance Act Amendments of 1983."

Section 2: Section 1309 of the National Flood Insurance Act of 1968, as amended (Public Law No. 90-448, 82 Stat. 577) is amended--

(a) By adding at the end thereof the following new subsection:

> "(c) The Congress shall periodically review the authority of the Secretary under this section and determine the extent to which it is adequate and necessary for carrying out the flood insurance program. Such review shall include a finding whether the authority granted to the Secretary by this section should be continued."

(b) In subsection (a) by (i) inserting the words "paying only extraordinary losses incurred in" between the words "of" and "carrying" in the first sentence; (ii) striking the words "request the approval of the President" and inserting in lieu thereof the words "exercises his authority to borrow funds" in the second sentence thereof.

(c) In subsection (b) by adding the following new sentence at the end thereof:

> "Request for annual appropriations under section 1310(g)(1) shall include an amount equal to the total funds borrowed by the Secretary."

Section 3: Section 1310 of the National Flood Insurance Act of 1968 is amended by adding at the end thereof the following new section:

> "(g) The Secretary shall estimate in each fiscal year the 'deficiency costs' of the flood insurance program for the next fiscal year. Based on this estimate,

the Secretary shall submit a request for appropriations for the next fiscal year that is sufficient to pay the estimated 'deficiency costs' of the program in such fiscal year. Such request shall be submitted along with the annual budget required by subsection (e).

"(1) In the event that the funds appropriated or collected under subsections (b)(2), (b)(3), (b)(4), (b)(5), and (b)(6) of this section are not sufficient to pay all the costs of the program in any fiscal year; or the Secretary exercises his authority under section 1309 to borrow funds during any fiscal year; the Secretary shall before the end of such fiscal year submit, along with his request for appropriations to pay the estimated 'deficiency costs' for the next fiscal year, a request to Congress for appropriations sufficient to pay all the 'deficiency costs' of the program for any current fiscal year, and to repay total borrowings from the Treasury for any such fiscal year, if applicable. 'Deficiency costs' are the difference between the amounts received by the flood insurance fund under subsections (b)(2), (b)(3), (b)(4), (b)(5), or (b)(6) of this section, and all the applicable costs and operating allowances expended to carry out the flood insurance program during a fiscal year."

SECTION-BY-SECTION ANALYSIS

Section 1. Title of enactment. The purpose of these amendments is to implement the legislative recommendations GAO developed during its review of the National Flood Insurance Fund. These proposed amendments are designed to improve Congress' oversight and control over the expenditures of the National Flood Insurance Program.

Section 2. GAO concludes that Congress needs to consider whether the flood insurance fund is now the appropriate method for funding the flood insurance program. The amendments set out in section 2 are designed to improve Congress' control over the flood insurance fund should it determine that the fund is still the best vehicle for financing the program. This section amends the act to: (a) require periodic congressional review of the borrowing authority of the Secretary; (b) limit the Secretary's borrowings from the Treasury to pay for only extraordinary losses

and require notification to Congress if borrowing occurs; (c) require the Secretary to seek annual appropriations from Congress to repay in the next fiscal year the Treasury funds borrowed during the current fiscal year.

Section 3. In addition to providing that the Secretary must seek appropriations to repay Treasury borrowings, this amendment is intended to require the Secretary to estimate and to seek annual appropriations to pay for the "deficiency costs" of the flood insurance program. "Deficiency costs" are the difference between the amount received by the flood insurance fund under subsections (b)(2), (b)(3), (b)(4), (b)(5), or (b)(6) of section 1310, and all the applicable costs and operating allowances expended to carry out the flood insurance program. Thus, for example, where the rates charged are insufficient to pay for annual loss claims and costs for these policies, a "deficiency" or "subsidy" occurs in the program. Under such circumstances, the Secretary must request appropriations for the next fiscal year to pay for the current year's deficiency, and to pay any estimated deficiency for the next fiscal year.

PROPOSED AMENDMENTS TO THE

NATIONAL FLOOD INSURANCE ACT OF 1968

TO FINANCE FLOOD INSURANCE THROUGH A DIRECT APPROPRIATION

Section 1. This act may be cited as the "National Flood Insurance Act Amendments of 1983."

Section 2: Section 1309 is repealed.

Section 3: Section 1310 of the act is amended by striking all that follows "Treasury of the United States" and inserting in lieu thereof the following: "an Emergency Flood Insurance Loss Fund (hereinafter referred to as the "fund") which shall be funded and available without fiscal year limitation to pay unanticipated losses or expenses resulting from the occurrence of an emergency, or for other purposes authorized by Congress in appropriation or other acts. The Secretary shall report to the Committee on Banking and Currency in the House and to the Committee on Banking, Housing and Urban Affairs in the Senate at any time he exercises his authority to make payments from the fund. Further, the Secretary shall seek in his next request for appropriations sufficient funds to replenish the fund if he exercises his authority under this section."

"(b) An annual business-type budget for the flood insurance program shall be prepared and transmitted each fiscal year to Congress along with the Secretary's request for appropriations. Such budget shall include a statement of the premiums, fees, and other revenues received from carrying out the flood insurance program (including appropriations) and shall separately show the "surplus or deficiency," as defined in section 1370(d), for (i) the flood insurance program in general, (ii) the insurance provided at risk premium rates, and (iii) the insurance provided at less than risk premium rates. The budget shall be submitted to the Committee on Banking and Currency in the House and to the Committee on Banking, Housing and Urban Affairs in the Senate in the fiscal year that preceeds the year to which the budget is applicable. Congress shall consider and enact the budget in the manner prescribed by law for wholly-owned Government corporations."

Section 4: Section 1376 is amended--

(a) In subsection (a) by: (1) striking the entirety of subpart "(2)" and "(2)(A)" and "(2)(B)"; and (ii) striking the number "(3)" in subpart (a)(3) and redesignating it as subpart (a) "(2)."

(b) In subsection (b) striking the words "without fiscal year limitation" and inserting the following in lieu thereof: "for use on a fiscal year basis."

Section 5: Section 1370 is amended by adding at the end thereof the following new subsection:

> "(d) The term 'surplus or deficiency' (as used in section 1310(b)) means (i) the sum of all appropriations, receipts, premiums, or other revenues collected during a fiscal year less (ii) the sum of all applicable costs and operating allowances disbursed during the same fiscal year."

SECTION-BY-SECTION ANALYSIS

Section 1: Title of enactment. The purpose of these amendments is to implement the legislative recommendations GAO developed during its review of the National Flood Insurance Program. GAO concludes that the Congress needs to gain more direct control over the expenditures of the flood insurance program. If the Congress determines that the flood insurance fund is no longer the appropriate mechanism for financing the program, GAO recommends that the Congress amend the act to require direct appropriations to finance the flood insurance program.

Section 2: This section implements the aforementioned recommendation by abolishing the National Flood Insurance Fund and by operation making the program's funding subject to direct appropriations.

Section 3: To maintain flexibility in the funding of the program, an emergency loss fund is established which would be used to pay for unanticipated losses and expenses resulting from the occurrence of an emergency, or for whatever purposes Congress might specify in appropriation or other acts. While no attempt is made to describe the conditions under which the Secretary may determine an "emergency" exists warranting use of the fund, it is anticipated that the fund would normally be

available to supplement appropriations when, due to the occurrence of unforeseen circumstances beyond the control of the Secretary, available financial resources are or will be depleted. Funding levels would be maintained by direct appropriations requests each fiscal year if the fund is used.

This section also requires the Secretary to prepare and submit an annual business-type budget each fiscal year along with his request for annual appropriations. A requirement is established for the budget to show the "surplus or deficiency," as defined in new section 1370(d), for (1) the overall flood insurance program, (2) the class of insurance for which risk premium (actuarial) rates are charged, and (3) the class of insurance for which less-than-risk premium (actuarial) rates are charged. The purpose of this requirement is to give the Congress the information it needs to determine the extent to which Federal funds subsidize the overall flood insurance program and, at a minimum, two classes of policies for which different rates are charged.

Section 4: This section sets out technical amendments that conform existing provisions of the act to the elimination of the flood insurance fund and the conversion of the program's funding to the direct appropriation method.

Section 5: A definition of "surplus or deficiency" is added to the act by this section to make it clear that the "surplus or deficiency" set out in the budget for the overall program and for at least two classes of insurance should be calculated by totaling all revenues received and subtracting the sum of all applicable costs and allowances.

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CONVERSION OF EMERGENCY COMMUNITIES

Senator HECHT. Thank you. Mr. McLoughlin, how many of the remaining 7,300 emergency communities can FEMA convert to the regular program without detailed mapping?

Mr. MCLOUGHLIN. Senator, may I pause just for a moment and introduce my colleague who's with me, Mr. Richard Krimm.

Senator HECHT. It's nice to have you here.

Mr. MCLOUGHLIN. He's the Director of our Office of Natural and Technological Hazards.

The specific response to your question is there's about 7,300 communities that have not been converted yet, our best estimates are right now that about 3,000 or 3,100 communities could be converted. The process we use in that conversion is to send someone from our regional office to the local community to meet with the officials, to go through a series of steps with them to determine whether or not there is little likelihood of development over the next few years, and assuming for the moment that the report shows no continued development, then we can convert those communities in about a year.

Senator HECHT. Thank you. Ms. Whilden who will be representing the National Association of State Flood Plain Managers has submitted testimony which states that 40 percent of the remaining communities could be converted to the regular phase based on flood boundary maps. If this is true, has FEMA taken this into account in requesting 3 additional years for mapping the remaining communities and is it reflecting the cost estimate of $153 million?

Mr. MCLOUGHLIN. Yes, Senator, it is. We have had discussions with the State Flood Plain Managers Association. I would need to look at the testimony to be sure what the 40 percent represents, but I believe it's 40 percent of the 10,000 communities that are not participating right now, and if that's the case, then our estimates are not very far apart.

Senator HECHT. We understand that FEMA considered in 1979 using an accelerated conversion process but abandoned it in 1981 before it was implemented. Can you explain why?

Mr. MCLOUGHLIN. Sir, I don't believe that's an accurate statement, that we abandoned it. We have been looking at accelerated conversions and we are looking at accelerated conversions right now and it is our intent for about 3,000 remaining communities to be converted under these procedures.

Senator HECHT. How many of the communities which have already been mapped have required subsequent mapping? Under GAO's proposal, FEMA would have the authority to remap communities which feel that the mapping results are inaccurate. Wouldn't this allow these communities which have a preconceived level of risk to obtain a more detailed map while at the same time avoid unnecessarily mapping of uninterested or low risk areas?

Mr. MCLOUGHLIN. Senator, we have a continuing program of restudies based on a variety of criteria. Clearly, the restudies are a necessary and continuing part of the program. We don't believe that the restudy area though is adequate to address the needs of approximately 4,000 communities which have not had a detailed study to date.

Senator HECHT. Mr. Dodge, if the Congress were to adopt the General Accounting Office's proposal to transfer the emergency communities into the regular program, how would this affect the flood plain management in these areas?

Mr. DODGE. It would not affect it greatly and I think I would ask Mr. Noel, to my right, to elaborate on that.

Mr. NOEL. Senator Hecht, as has been noted by both Mr. McLoughlin and Mr. Dodge, these remaining communities are generally considered to be areas which are not developing very much. So the need for detailed information such as how high the flood waters would come in a 100-year flood, is considered to be fairly low. More importantly, because of some improvements that the Federal Insurance Administration has made in the rate setting in these areas, there would be insurance incentives for people to elevate their properties once they moved into a regular program. So an important part of the program that's now handled by rules when you move into the regular program with the detailed map would be handled with the insurance aspect.

Senator HECHT. Are most of the remaining communities developing areas?

Mr. NOEL. No, not based on our review. We find they are not.

Senator HECHT. Do you feel that the levels of risk can be determined by the flood hazard boundary maps? Are these maps sufficient to set actuarially sound insurance rates?

Mr. DODGE. Yes, however, in some communities, Mr. Chairman, you may need the detailed study that provides a more detailed flood insurance rate map; these are the areas where you would expect to see development. The vast majority of the emergency communities however, would not, nor would we, require detailed mapping and you could use the flood hazard boundary maps as rate maps in these areas primarily because there isn't a great need for the detailed distinctions that you get through the detailed mapping process.

Senator HECHT. Why is FEMA's proposal to eliminate the Federal subsidy such a pronounced departure from how the program was administered?

Mr. DODGE. I'll ask Mr. Noel to answer that.

Mr. NOEL. When the program was established, Senator, there was a conscious decision made by the early FIA administrators to provide a fairly heavy subsidy to existing properties for people who weren't aware of the risk when they bought. The administrator didn't want to penalize these people when they came into the program. To develop a self-sustaining program by fiscal 1988, it's our view that there will have to be some changes made to these rates which have been relatively constant over the life of the program. Because of the way FEMA collects the data, it's difficult to estimate how much the rates will have to go up, but I think it's safe to say there will have to be some substantial rate increases or some fairly substantial declines in the coverage.

As a result, we think that this is a pronounced departure from how the program had been administered and in our report we asked the Congress to consider giving FEMA some guidance about the matter of subsidy. As the act is now, FEMA can make decisions about the level of subsidy.

Senator HECHT. Mr. McLoughlin, would you want to comment on that?

Mr. MCLOUGHLIN. Senator, I'm not that familiar with the Federal insurance program. Mr. Bragg is our insurance administrator, but I would be glad to provide something for the record if you would like.

Senator HECHT. One last question, Mr. Dodge. Can you give some examples of how the lack of requirement to regularly request appropriations to repay borrowing reduced the Congress ability to oversee the flood insurance program?

Mr. DODGE. That's another question, Mr. Chairman, I'm going to defer to Mr. Noel.

Senator HECHT. It's nice to have you here today, Mr. Noel.

Mr. NOEL. The way the national flood insurance fund is set up now FEMA is not required to come in regularly and request appropriations to repay moneys that it borrows from the Treasury. For the first 10 years or so, the program financed its losses due to both the subsidy and to the inadequate rate making by borrowing from the Treasury. The result was that in late 1981 the program had used up the billion dollars in borrowing authority that Congress had given it and it came to the Congress and asked for a $500-million appropriation to pay claims.

During that time the GAO issued a number of reports which pointed out weaknesses in ratesetting and data collection that would have identified some of these problems. We feel that a regular request for appropriations would provide the right kind of forum for congressional oversight.

Just to provide some balance, I think it's important to recognize that within the last few years FEMA has come in regularly for appropriations, openly disclosing where the money is going and what is needed.

Senator HECHT. One last question and you can determine who you want to answer it. Can you explain briefly the results of the GAO's April 1982 report entitled "The Federal Crime Insurance Program—An Overview?"

Mr. DODGE. Yes, Mr. Chairman. This is essentially an information report not intended to draw any conclusions or offer any recommendations to the Congress on the crime insurance program. It stands as our offering of data that we collected to be used by the Congress as it best sees fit. We do note in that report that about 72,000 policies had been issued as of the time we made our study. We felt that that indicated some need for the existence of the program. However, we also noticed, as have previous witnesses, that a high percentage—we found 71 percent—of the policies are concentrated in three States and we therefore implied the question of whether or not this program meets a national need. We do wrestle some with the question of affordability of rates and whether or not you can have a viable Federal program to address the lack of a private program and still offer affordable rates.

Senator HECHT. Thank you very much.

Senator Hawkins.

FLOOD INSURANCE IMPORTANT TO FLORIDA

Senator HAWKINS. As you all know, the flood insurance is extremely important to Florida. I think we have had over 11,000 claims since the inception of the program. One of the many criticisms of this program came from Marian County, Fla., which is Ocala, the new horse breeding country of the South. This county commission really did pinpoint some problems that you should be aware of.

This board of county commissioners met and they felt that the procedure established by the Government in notifying the local government of the map appeal process is somewhat vague and should be amended. Marian County did receive legal notice of the map appeal procedure. The notice was not adequate enough to apprize the board or the public of the problems that arose subsequent to the end of the appeal hearing.

A major problem of the flood maps of Marian County—and this is a common thing throughout our counties that responded—is the lack of data on the maps. The maps of Marian County do not have all the 100-year flood plain elevations nor does it have photogrammetry details which makes it impossible to locate a specific parcel of property. Additionally, there are literally hundreds of errors in the Marian County flood maps, the most notable one being the map of the Orange Lake-McIntosh area which shows the Okawaka River in downtown McIntosh, which is quite a big error.

Now the board of this county would like assistance in obtaining a change in the map appeal procedure, which might require the Federal Emergency Management Agency to hold a public hearing, in conjunction with the local government being required to adopt a flood prevention ordinance, and explain the detailed flood maps and any apparent deficiency in the same. I'm not saying I endorse the public hearing concept. Maybe you might have a workshop. It's very popular to have workshops in Florida in the wintertime. We highly recommend it depending upon the weather up here.

What comment would you have on suggestions like that?

Mr. MCLOUGHLIN. Senator, there are many items that you addressed in your comments. Clearly, our process is intended to provide an opportunity for local officials and for us to meet with the local officials—in fact, it includes a meeting with the local officials and State officials if they are available to do just what you said—give the local community an opportunity to understand what the map is and to determine whether or not there's a major disagreement with local data. Clearly, if there's a river in the wrong place, that I assume is our error, but the process is intended really to provide an opportunity for the local officials to be part of the process.

Senator HAWKINS. Even though they did not have time before the end of the appeal process, they can still appeal to you?

Mr. MCLOUGHLIN. There's a 90-day appeal process that's statutory. After that period, at any time when a community can demonstrate that there are errors in the map, or that significant changes have taken place, we will be glad to sit down and take a look at it with them.

Senator HAWKINS. Another suggestion they had, which I really liked, was the proposal that you could have a certified statement

from a registered engineer, that a certain parcel of land is not prone to flooding and to automatically remove that said parcel from the flood-prone area upon receipt of the engineer's certificate by the original office of FEMA. Would you have any comments on that?

Mr. McLoughlin. Senator, we do that now. We have a procedure by which we can make amendments to our maps on an individual case basis. This procedure results in a letter of map amendment, exempting the individual property owner.

Senator Hawkins. By a certified engineer?

Mr. McLoughlin. Yes, FEMA makes a determination based on the data that's provided to us by the individual who is seeking the letter of map amendment. It does not necessarily have to be a certified engineer, but that certainly is one option.

Senator Hawkins. Well, we have many areas, as you're well aware of, in our State, that during the dry years builders build everywhere and the oldtimers would tell you that's going to be a lake someday and it used to be a big deep lake and now it's got rolling hills. Where do you think you get hills in Florida? The old hills came from the bottom of the lake to the top of the lake when it dried out and, sure enough, when the rains came, those homes were all evacuated. The same thing happened in California last year. We had that huge flood in San Diego and the cab driver that was taking me to a speech said, "I could have told them. I used to swim in that river right where Bullock's store was. That whole mall was a river when I was a kid." It just seems that weather patterns being what they are, maybe we'll get better information if we sell the weather information—I doubt it seriously.

Mr. Dodge. I might add, Senator, that FEMA sometimes exercises other options in a situation like this where new information is available, or when there is some basic problem with the map. They can restudy the whole situation and they do this quite frequently. It may be that if there are serious problems with the map in any area, that you might propose the option of a basic restudy to produce a new map.

Senator Hawkins. When you were answering the chairman's questions about raising the rates so there wouldn't be so much subsidy in the total program, that kind of alarms me as an insurance holder. I've never had a claim and always pay my policy—just like I've never had a claim on my driver's insurance either—why should that affect the ratepayers and policyholders who have never had a claim? It really should not be distributed across the broad base of all the policyholders because a certain area had an emergency.

RATES A CATCH-22

Mr. Dodge. This is a real problem because in a way it's a catch-22. In a way you want the rates to remain attractive and affordable. At the same time, under all the pressures of these times you want to try to make ends come closer to meeting in these programs. We ask in one of our reports whether it's appropriate to leave that judgment entirely to FEMA, and suggest that the Congress might want to take part in the process of making that judg-

ment, to decide whether or not a certain level of subsidies or a certain duration of subsidies should be kept in force over a long period of time.

Senator HAWKINS. As in your statement, maybe Congress should appropriate a certain amount of money to fund that program. It may have a surplus in it at the end of the year, if we have good weather or good fortune and could tide it over.

Mr. NOEL. That's one of the things that we suggested. It also might be possible to have the Congress make a decision about the percentage of subsidy that would be received. For example in the crop insurance program, farmers get a percentage subsidy of their loss from the Federal Government.

Senator HAWKINS. I don't want any crop conversation in this particular record. I just received a letter from a man who wants to know how much he's going to make by not planting corn on his land under the new PIC program. He wants to go into the not-planting-corn program because it seems to be very profitable. Let's not get agriculture mixed up with this particular thing. That's the worst program we could possibly compare this to.

Supposedly this started out as an emergency program, uninsurable by normal insurance companies who like low risk and high premium. So I think that you're right on target when you say that maybe we should look at it as an appropriation process by the will of Congress, as Senator D'Amato expressed earlier on the riot insurance. I thank you all for being here.

Senator HECHT. Thank you very much.

We will continue with the next panel. We're going to continue right on through. We're not going to break.

Ms. Whilden, are you ready? We look forward to hearing from you.

STATEMENT OF MARGUERITE M. WHILDEN, NATIONAL ASSOCIATION OF STATE FLOOD PLAIN MANAGERS

Ms. WHILDEN. I'd like to give a summarized version of my testimony and ask that my written version be submitted for the record.

[The complete statement follows:]

STATEMENT OF THE ASSOCIATION OF STATE FLOODPLAIN MANAGERS

By MARGUERITE M. WHILDEN

On behalf of the Association of State Floodplain Managers it is a pleasure to assist you in your review of certain activities of the National Flood Insurance Program. Our Association was organized in 1977 and has worked closely with the National Flood Insurance Program in improving floodplain management at the State and local levels.

As you requested we will address three major issues: the importance of the current National Flood Insurance Program (NFIP) to the states, the General Accounting Office (GAO) proposal to eliminate the Emergency phase of the National Flood Insurance Program, and the Federal Emergency Management Agency (FEMA) request for extending the flood mapping studies and the Emergency phase.

1. The Current National Flood Insurance Program

We support the National Flood Insurance Program in its original concept - to provide federally subsidised flood insurance to reduce public expenditures and losses to the private property owners in exchange for regulations to mitigate future flood damages. We believe it has been effective in reducing flood losses.

The NFIP is consistent with most State floodplain management efforts. As you may know, over two thirds of the states regulate or establish minimum standards for regulation of flood hazard areas.

We appreciate the recent efforts of FEMA staff to cooperate with us more readily and consult with us more often. At times in the past we had difficulties defending the NFIP to our local communities because we were not adequately involved or informed of FEMA plans.

FEMA Regional offices have also shown a greater willingness to tailor their assistance efforts to their particular states so that states in turn can provide the needed assistance to their local communities. However, not all FEMA Regions can provide the same service to the states nor have they been successful in developing a strong Federal-State team. The Natural and Technological Hazards Division of FEMA Region III, under the direction of Walter Pierson, provides an excellent example of the services and benefits Regional offices can and should provide. Mr. Pierson and his staff have carefully involved the states in conducting workshops, correcting flood studies, reviewing building and development permits for states and communities, assisting and evaluating local implementation and enforcement, along with many other special services. These efforts are being hindered, however, by lack of staff and funds. We hope the flood management staff will be restored at the Regional level so that we can receive the cooperation and attention which a Regional perspective can provide.

The states are also appreciative of the training and education we have received through FEMA-sponsored conferences, workshops, and informational materials. However, we feel some very important professional groups have been neglected. Much of our day-to-day activities involve assisting insurance agents, realtors, lenders, builders, and developers with flood insurance and floodplain management problems. We need more training and education at the private professional level. These people are the link between the NFIP and the public and they are often eager to learn how to provide better services to their clients.

In general the current National Flood Insurance Program supports our state-level efforts to improve flood hazard management and lessen the costly burden of flood disasters.

2. The General Accounting Office Proposal

Unfortunately the GAO proposal to eliminate the Emergency phase of the NFIP is an oversimplified approach to a complex problem. Simple elimination is not likely to achieve the desired savings and will undermine state floodplain management. There are two methods proposed by GAO for eliminating the Emergency phase of the NFIP: one is to allow the Emergency phase to expire as presently scheduled in August of this year and the second is to immediately convert all Emergency phase communities into the Regular phase of the NFIP without a detailed flood mapping study. Both proposals, as they now stand, have problems.

The first method is unacceptable to us because there are too many unanswered questions. Would these communities simply be dropped from the Program? Would flood insurance still be available in these communities? If flood insurance is available, must these communities regulate floodplain development? If so, to what standards and what incentives would there be to insure enforcement? How much insurance coverage would be available to the residents of these areas? And lastly, but perhaps most important, would not the savings expected by ending the Emergency phase be negated by the administrative problems which would inevitably result?

The second method, an immediate conversion of all Emergency phase communities into the Regular phase, is unacceptable because we feel it will create more problems in the short-term and greater expense in the long-term. The proposed single advantage is that this conversion of communities will eliminate the need for additional new flood mapping studies and thus save the Federal government a substantial amount of money. The need for flood mapping studies will not go away overnight.

There are several disadvantages. Entry into the Regular phase of the NFIP provides roughly 5 times the amount of flood insurance coverage of the Emergency phase and for this additional benefit what does FEMA get or expect in return for this additional liability? Without a detailed or improved flood mapping study how will a converted community implement better floodplain management?

We know many of these communities are expanding and are in dire need of a detailed flood mapping study. We assume these converted communities would be expected to regulate to Regular phase standards in order to comply with the National Flood Insurance Program statutory requirements. Will there be a different set of standards for these communities without flood mapping studies or will they be expected to generate the necessary data themselves? We believe FEMA must provide an equitable means to secure such data for these areas.

Perhaps the greatest disadvantage is that an immediate conversion would not allow for an organized progression, hence it would create serious problems for FEMA, the states, and most importantly, the communities involved. Here again, I am afraid the problems created would outweigh the projected benefits.

Our major point regarding the GAO proposal is that we cannot support the concept of providing federally subsidized flood insurance to communities which

do not adequately regulate floodplain development. The success of the National Flood Insurance Program is contingent upon insuring that future construction will not be subject to flood hazards. If the GAO proposal were modified to meet this objective we could reconsider.

3. Federal Emergency Management Agency Request

There is an equitable and practical approach available. We endorse the FEMA request to extend the Emergency phase of the NFIP and gradually convert all communities to the Regular phase within four years. We understand that this approach would involve a combination of three flood mapping study techniques described below.

We believe that much of the success of the federal and own state flood hazard mitigation programs is due to FEMA's flood mapping studies and restudies effort. In spite of dwindling State and federal budgets, we need flood mapping studies to implement floodplain management and promote the sale of flood insurance. The key federal role is to provide flood mapping studies and flood insurance; the states and locals are responsible for the floodplain management.

We endorse FEMA's proposal for continued, but modified, flood mapping studies as part of an orderly conversion process for remaining Emergency phase communities.

With the proposed FEMA approach, a portion of the Emergency phase communities would receive a detailed flood mapping study, a second portion would be studied using existing data from local, regional or state sources (Existing Data Study), and a third portion would be converted to the Regular phase after minor modifications are made to their existing Emergency phase Flood Hazard Boundary Map.

Based on surveys made by the Association of State Floodplain Managers, numbers have been generated which indicate the following: approximately 40% of the communities currently in the Emergency phase need a detailed study at this time; approximately 20% of the communities could be provided with studies using the existing data study process; and approximately 40% could currently be converted to the Regular phase based on the Flood Hazard Boundary Map (this assumes that some minor modifications to the maps could be made to correct obvious inconsistencies and inaccuracies using field observations as the basis).

Our figures are estimates based on a sampling of our member states. We understand FEMA plans to conduct a detailed evaluation of community conversion and mapping needs which will aid them in their flood mapping study budget requests and give them an accurate picture of their task. We feel 1987 is a realistic target date for converting all Emergency phase communities in an equitable manner. We pledge our utmost support and cooperation to FEMA in developing an implementation strategy and schedule for this important task.

State	# Identified Communities	New Studies as % Emer & N.P
Colorado		100.0
Nebraska		19.3
Illinois		31.2
Iowa		32.9
Texas		20.0
Wisconsin		41.6
Indiana	404	10.0
Pennsylvania		10.7
California		38.3
Florida		100.0
Maryland		48.7
Georgia		35.0
New Mexico	89	50.0
W. Virginia	257	0.0
Virginia	275	30.0
Delaware	42	0.0
N. Dakota	246	52.0
Louisiana	334	11.7
Kansas	446	11.5
Missouri	547	35.0
Wyoming	83	50.0
Utah	202	10.0
Massachusetts	350	6.0
Maine	1009	10.0
Vermont	272	10.0
New Hampshire	221	20.0
Rhode Island	39	10.0
Ohio	732	57.4
Michigan	524	18.5
Minnesota	627	6.8
Mississippi	296	76.0
Alabama	375	100.0
S. Caroline	216	75.0
Tennessee	346	85.0
N. Caroline	368	100.0
Kentucky	309	100.0
S. Dakota	160	0.8
Montana	127	18.0
Nevada	32	40.0
		1571.4
		39 = 40.3

40.3% X Total Emer. Prog.(11187) = 4508

TESTIMONY OF Ms. MADHU BERIWAL
Floodplain Manager
Department of Urban and Community Affairs
State of Louisiana

With almost $100 billion in flood insurance coverage in effect the National Flood Insurance Program (NFIP) is one of the largest federal programs. Almost 20,000 communities in the nation have been identified as being flood-prone. In 1982, approximately 85 percent of these communities were participating in the NFIP, with 10,500 in the emergency phase and 6,500 communities in the regular phase. About two million policies are in force, affecting over seven million persons. Millions more are indirectly affected through federal subsidization of the program. In fact, the nation is inextricably and inexorably enmeshed with the consequences of flooding. Each flood triggers a "ripple-effect", affecting areas and the lives of people far beyond the reach of flood waters.

Hence, it is crucially important to objectively and critically evaluate changes in this national program to ameliorate the effects of floods. Options born of incomplete examination may prove to be worse than castles in the sand—encouraging a false sense of achievement and security that may be rudely destroyed with the first wash of surging waters.

In my estimation, the option recommended by the General Accounting Office to curb the spiraling deficits of the National Flood Insurance Program is like a castle-in-the-sand. Well-meaning though the efforts of the GAO have been, the wholesale conversion of emergency program communities into the regular program without detailed mapping might be a decision that, if implemented, may soon be regretted. I will strive, in my testimony, to present to you the inherent weaknesses of this policy and also suggest some personal recommendations for the National Flood Insurance Program.

The GAO option would impact the approximately 7,000 communities currently in the emergency phase of the NFIP. These communities constitute about one-third of all flood-prone communities. A League of Women Voters study in early 1982 estimated that two-thirds of all communities we e awaiting detailed maps. Whatever the data source, the GAO option would affect a large proportion of all flood-prone communities in the nation. Adoption of the GAO recommendation would not constitute a marginal change in the NFIP. It would drastically alter the character and effectiveness of the program. However, the applicability of the GOA suggestion is severly limited in about 700 coastal communities. Together with the almost 1,200 communities in 1982 that were in the regular program without detailed maps, the cessation or slowing down of detailed maps would greatly affect the NFIP. I will attempt to briefly address the anticipated effects of the GAO option on the health, safety and welfare of citizens, national flood losses and flood-related damages, development trends, economics of the National Insurance Program, and the hydrologic characteristics of flooding.

SAFETY

It is my estimation that implementation of the policy recomemeded by the GAO would not increase the safety of citizens, and in fact could make life more hazardous for floodplain residents. Since the floodplain management regulations required under the GAO option are minimal, development in the Special Flood Hazard Areas would not be curtailed. Even worse, the type of development would not be commensurate with the flood hazard. Elevation of structures to the base flood elevation would not be required and compared to the regular phase, savings

in insurance premiums to individuals would not be incurred through elevation. The building of homes at grade elevation would greatly increase the threat of loss of lives in the event of flood. As the maximun amount of insurance coverage would be made available, The National Flood Insurance Program would actually spur flood plain development. This would raise the number of people at risk and increase flood heights substantially, putting these individuals at greater risk (Hydrologic studies have revealed that flood height are increased from two to six times due to urbanization in small watersheds.).

Preliminary maps of these communities would not indicate degrees of flood hazard (i.e., B and C Zones), encouraging further invasion in these areas and accerbating the flood problems. Although "best available data" is expected to be used in emergency phase communities, past history has revealed that such information will not be used unless mandated or, worse, data that most minimizes flood hazards will be accepted as the basis of elevation decisions. Local officals are aware of the flood hazard, especially since the inception of the NFIP. Studies conducted in the State of Louisiana and elsewhere have documented a surge of flood awareness in communities that have joined the NFIP. Despite this, the tenuous relationship between awareness and behavior still remains a mystery. Also, since the frequency of flood events is lower for each community than for the nation, flooding often receives a lower priority in resource allocation at the local level than at the national level. The personal consequences of decisions are also higher at the local level than at the national level. All these factors suggest that minimal implementation of floodplain management regulations would be the rule rather than the exception. The potential for development in the floodplain of emergency phase communties is high. In fact, analyses performed by the Louisiana Department of Urban and

Community Affairs have revealed that one of the principal characteristics defining the Emergency phase communities from those in the Regular Phase is the extent of existing development in the floodplains. Improved warning systems have reduced the risk of death from floods. Greater numbers would face greater risks from floods if the GAO policy is implemented. The absence of safety issues present in the questions asked by the GAO document the minimal attention paid to this critical human problem.

FLOODPLAIN MANAGEMENT AND ECONOMIC PERSPECTIVES

Insurance is always based on the premise that losses will occur. The National Flood Insurance Program has paid claims that amount to three times as much as it has received in premiums. Yet, at last count, this year, the NFIP has finally run out of red ink and stands solvent. Between the fears of further deficits and the current rosy situation lie the truths of the economics of the program.

During the period 1968 to 1981, studies reveal that the National Flood Insurance Program expended over $3.6 billion, and received $866 million in premiums—a seeming net loss of over $2.8 billion. However, studies by the U. S. Water Resources Council estimated that flood damages in the year 1979 alone reached $3.8 billion. A substantial portion of these flood losses would have been paid by the federal government through disaster relief, loans, and other programs. A saving of at least $866 million was possible, with future reductions in the increase in flood damages possible through floodplain management regulations and increased premium collections. The alternative to the NFIP is a reversal to the even more expensive strategy of high relief costs and billions of dollars of expenditure on structural, public-works projects.

A brief examination of the NFIP spending sheds light on the deficits. Subsidization of insurance premiums accounted for the largest share of the budget--about 40 percent in the period 1968 to 1981. Several reasons lie behind this high subsidy. Principally, actuarial rates cannot be charged in the very high-risk areas. For example, a rate of $2,000 annual premium for a $20,000 structure in New Orleans was quoted by Lloyds of London in the late 1960s. There would be no economic incentive for flood insurance if premiums were based on actual risk. Secondly, the NFIP regulations include a "grand-father" clause that subsidizes all structures built before the inception of the program or before detailed mapping . Since a majority of insured structures in the floodplains were built before 1968, the subsidization costs for such structures are immense. Emergency-phase communities also enjoy the benefits of subsidization, and all structures built before detailed mapping will be subsidized for the life-span of the structure. Hence, the costs entailed in financial protection of these structures will continue into the future, further compounding the ratio of premiums to claims. Actual decreases in flood claims will only occur after these structures are destroyed or "substantially-improved". Implementing the GAO option may improve the financial picture in the short-term, but the difference will be made up in increased development and lack of enforcement of floodplain management regulations.

As new structures are built under the emergency phase of the program with few attendent controls, flood claims arising from damages to these will continue to be substantial and will remain a financial drain on the NFIP.

Recent premium rate increases were, therefore, necessary and have facilitated the present financially-stable position of the NFIP.

The next major category of expenses is the amount of claims. These have escalated during 1968 to the present. The increase can be attributed to development in floodplains, the increase in the total number of policies and the amount of coverage, and some abuses of the NFIP by floodplain residents. The NFIP, with its regulatory structure and subsidies, cannot attain an absolute decrease in total flood losses in the near future. The NFIP regulations do not prohibit development in the floodplains; they only restrict the type of development that can occur. Under the GAO option, the total value of claims can be expected to rise with the lack of floodplain management regulations in the substantial number of emergency phase communities.

The next major category is inevitablty a part of the NFIP--mapping. Mapping costs during 1968-1981 accounted for less than 15 percent of the total program budget. In the federal quid pro quo of insurance and regulations, mapping is the vital link on which both insurance and regulations are based. The reduction of mapping efforts in emergency phase communities will not substantially affect the funds required for flood insurance studies, and lack of such detailed information will severly hamper efforts to reduce total flood damages. There is a high "obsolescence factor" present in flood insurance mapping. Re-studies are required as new issues become important (e.g., coastal wave-height elevations, alluvial fans, erosion, subsidence, etc.), new data is generated, substantial development occurs in communities changing the hydrologic conditions of flooding and thus risk factors, flood protection systems are put into place, and land is annexed by communities and other physical changes affecting floods occur. All these factors are related to two dynamic forces: technological advances in the knowledge of floods and their management, and growth in flood-prone communities. They are aspects of "progress" and not subject to total cessation or even full

control by the NFIP. Re-study needs will continue indefinitely. A primary reason cited for the reluctance of the private industry to assume the program is mapping-related costs.

Appreciable savings will also not accrue from not preparing detailed maps for emergency phase communities. The savings realized would not make up for the indirect costs involved. Detailed maps constitute the one link between all the "actors" in floodplain management: lenders, insurance agents, developers, floodplain managers, policy-makers and the NFIP. In absence of concerted efforts to educate the public regarding flood risks and attendent losses, maps serve as the principal educational and policy-making tool. The level of information contained in the maps will be a ceiling on the awareness of flood hazards for most floodplain residents. Without detailed maps floodplain management regulations such as floodproofing or elevations would not be mandated, encouraging development that will be increasingly suseptible to flood damages. Both from an economic perspective and from a floodplain management perspective detailed mapping must continue for the viability, legitimacy and effectiveness of the National Flood Insurance Program.

I am personally not convinced that the expense constant of the NFIP could cover the total mapping expense. In my estimation, the expense constant may account for less than ten percent of the total mapping budget required. By 1981 $520 million had been expended on maps for approximately 10,000 communities. An amount close to that would probably be required to map the remaining 50 percent of flood-prone communities. The expense constant would generate less than $40 million annually.

Other costs involved would tend to rise as the number of policies increases and as more communites enter the NFIP. These costs (administrative, insurance

underwriting expenses, interest charges, adjustment expenses and operating costs) would be somewhat offset by the increase in premium collections.

There are potentials for saving within the National Flood Insurance Program. Misrating of policies seems to be a chronic problem. Misratings can be attributed to quality of mapping and some fraudulent assignment of lower-risk rates in high-risk zones. Two facts tend to aggravate this problem: the absence of any liabilty ascribed to insurance agents in most cases of misrating and the relative lack of controls on misrating by the NFIP. There is also no requirement for insurance agents to re-rate structures once maps are revised or zones changed. There could, additionally, be increased monitoring of claims for misrating.

Estimates indicate that about one-third of eligible policy-holders currently have flood insurance coverage. To increase the number of policies a number of actions can be taken: better marketing of flood insurance to floodplain residents, a greater involvement of the insurance industry in the selling of flood insurance, and provision of lower rates in lower-risk zones to encourage a pool of low-liability policies. Specifically, the emergency phase communities should be targeted for the sale of flood insurance. Four times as many policies are in force in regular phase communities than in emergency phase communities. The amount of coverage available in the emergency phase communities should be expanded to the total amount available in the regular phase. To reduce the liability that pre-FIRM construction poses, a "dual-rating" structure under scrutiny by the NFIP should be speedily adopted, i.e., different rates should be charged for pre-FIRM and pre-NFIP structures. This would also be equitable as the initial flood map does provide more information about flood-prone areas than existed before the NFIP. Included in this rating

structure for emergency phase communities should be strong elevation and floodproofing incentives.

In addition to changes in the insurance aspects of the NFIP, I would recommend some changes in the floodplain management regulations for both emergency and regular phase communities. A "financial preparedness" incentive should be explored by the NFIP, where disaster relief would be related to the number of policies, total value of policies in force, and other aspects of floodplain management. However, I would add a cautionary note in the exact mechanisms employed in gauging the extent of floodplain management efforts. Studies conducted at the Louisiana Department of Urban and Community Affairs have revealed that as flood hazard increases so do community efforts at control of flood damages, until a threshold is reached. Beyond this point, there is a reduction in effort as community resources cannot effectively manage the flood problem. Less expensive techniques of flood damage reduction are ineffective in such communities.

Another recommendation is to consider sliding insurance rates based on the performance of total watersheds in the management of floodplains. Since flooding is the result of changes within a watershed, such a strategy would encourage coordination efforts amoung local governments to reduce insurance premiums. A cooperative, comprehensive approach would result in greater reduction of flood damages than the current system. Other management measures include the mapping of claims to judge the need for focusing attention on high-loss watersheds. Again, studies at the Louisiana Department of Urban and Community Affairs reveal a pattern of loss based on watersheds.

Non-structural flood plain management should be more closely aligned with structural efforts to control flooding. Greater coordination is needed among

agencies that have responsibilities in either area. One of the specific actions that could be undertaken is to target high-loss areas for recommendations to community officials to seek funds to for structural and or non-structural projects.

State involvement in mapping, technical assistance and monitoring should be increased. Several states have the capability to conduct mapping studies, reducing the administrative costs to the NFIP.

I wish to address a concern in the development industry. A program to endorse initiative and innovativeness in floodplain development could be beneficial. Structures built to floodplain management standards and incorporating unique features designed to prevent flood damages could be certified through the Home Builder's Association, the American Institute of Architects or any other interested state or national group. This could be similar to the National Energy Watch (N.E.W.) homes and provide a better quality of floodplain development.

The last recommendation that I would like to make is to increase monitoring effectiveness through hydrologic checks. In consortium with the U. S. Geological Survey gauging stations above and below communities could automatically increase surface run-off increases. The increase in flood frequency and flood height measured by gauging instruments could be an objective measure of the effectiveness of floodplain management programs.

In closing, I would like to emphasize that the NFIP has achieved progress as measured by our studies and other research efforts. The National Flood Insurance Program has greatly increased the awarenss of floods in the nation. There has been a tremendous increase in the use of non-structural measures to manage floodplains since the inception of the program in 1968, especially in

communities where detailed studies and attendent regulations exist. However, research has also pointed out that for the regulations to be effective they have to be in place long before development pressures intensify. Providing detailed maps to emergency program communities may emerge to be one of the best opportunities for flood damage reduction that would be lost. Flood mapping has to strive for accuracy, ease of use and compability with local conditions. Each of these objectives would lead the NFIP to a financially-stable future and prevent needless agony to the nation's floodplain residents.

I would strongly urge you to continue the mapping effort. Human lives depend upon it. Floods are natural and will occur. All that can be hoped for is a reduction in flood damages. In fact, at this present moment major portions of the State of Louisiana are under a flood warning and a flood worse than the historic flood of 1977 is anticipated throughout South Louisiana. This committee's decision would affect all those citizens and people throughout the Nation.

MB:arh

TESTIMONY:FPM.1-B

Senator HECHT. Thank you very much.
Mr. Platt.

STATEMENT OF RUTHERFORD PLATT, PROFESSOR OF GEOGRAPHY AND PLANNING LAW, UNIVERSITY OF MASSACHUSETTS

Mr. PLATT. I am Dr. Rutherford Platt from the University of Massachusetts where I'm professor of geography and planning law, and I speak as a private individual, although I have served as a consultant with FEMA in the past. I am presently not under contractual relationship with them and I speak as a constructive critic.

I will skip over the first page and a half of my testimony since it's well covered by other speakers.

[The complete statement follows:]

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Testimony of Dr. Rutherford H. Platt
to the Subcommittee on Insurance of the
U.S. Senate Committee on Banking, Housing, and Urban Affairs
Re: The National Flood Insurance Program

April 8, 1983

My name is Dr. Rutherford H. Platt. I am a professor of geography and planning law at the University of Massachusetts at Amherst. I have been involved for several years with the National Flood Insurance Program as researcher, consultant, and hopefully a constructive critic. I presently have no financial or contractual relationship with the program and speak as a private individual.

Flooding in the United States is estimated to affect between 5 and 7% of our national land area including coastlines, riverine floodplains, and lake shores. The costs of flooding are difficult to estimate due to problems of consistent methods for identification, evaluation, and reporting. In 1966 average annual flood losses were estimated at approximately one billion dollars. By 1977, the U.S. Water Resources Council estimated that this total had risen to approximately 3.8 billion dollars, of which 1.8 billion represented actual increase in flood losses over and above inflation. Much of these losses was accruing in small metropolitan watersheds experiencing fast urbanization which are not amenable to large scale flood control works as traditionally conducted along main stem rivers by the U.S. Army Corps of Engineers.

Beginning in 1968, the National Flood Insurance Program has increasingly assumed a dominant role as the nation's primary response to flood losses. This response is two-fold in nature. First, insurance is made available to owners of flood prone property at rates significantly reduced by federal subsidy in many cases. Second, in order to qualify for this benefit, the community in which the property is located must participate in the National Flood Insurance Program.

Participation in the NFIP requires certain actions to be taken by local communities in response to studies and maps provided by the Federal Emergency Management Agency (FEMA). Initially, FEMA provided each of the approximately 20,000 communities with identified flood hazards with simple "flood hazard boundary maps" outlining the approximate area subject to a one hundred year flood. Although these maps were not necessarily based on detailed engineering studies, they did serve to identify areas in which flood insurance should be purchased and in which communities should exercise caution in granting building permits. Communities which signified their willingness to comply with certain minimum requirements could enter the "emergency program" and owners of property located therein could purchase inexpensive flood insurance at a flat rate up to specified levels of coverage.

The emergency phase ends for each community when it receives a detailed flood insurance study including a "flood insurance rate map" and a "flood boundary and floodway map". Following a period of time for appeal of possible errors in these documents, the community is expected to satisfy more stringent requirements for managing its flood hazard areas and thereby enter the "regular program". Otherwise it must drop out of the NFIP entirely and its property owners will subsequently lose their coverage.

The program initially was based on voluntary purchase of insurance. The Flood Disaster Protection Act of 1973 changed this basis to require purchase of flood insurance by anyone borrowing money from a federal or "federally related" instrumentality for the purchase or development of property in identified flood hazard areas. Furthermore, banks and other lending institutions were required to notify borrowers as to whether their property was flood prone and therefore subject to the mandatory purchase of insurance. Under a 1977 amendment, communities not participating in NFIP were removed from the prohibition on federally related lending since flood insurance could not be obtained by property owners in such areas. However, non-participating communities remain subject to a ban on federal disaster benefits should a flood occur.

Over the past 15 years of its existence, the National Flood Insurance Program has achieved remarkable progress. Approximately 17,000 communities are now participating in the program, more than 10,000 of them in the regular program. Regular program communities which generally have been required to adopt and enforce stringent floodplain management requirements now encompass about 85% of the total population. Furthermore, they include 96% of all communities with more than 200 flood insurance policies. Thus, a remarkable transformation has occurred in a very brief time. Whereas local floodplain management regulations were scarcely in existence as late as the mid 1960's, we now find new development to be subject to sensible limitation through building and land use regulations in most of the nation's major communities and metropolitan areas. This should substantially decrease the exposure and vulnerability of new development to flood loss. A further safeguard against unwise construction in hazardous areas is provided through the mechanism of "actuarial" rates for new construction and for increased coverage of existing structures. The widespread availability of flood insurance rate maps now facilitates the estimation of actuarial rates in preference to arbitrary flat rates which prevailed under the emergency program.

To date the National Flood Insurance Program, quoting to the General Accounting Office, has cost the nation's taxpayers 1.5 billion dollars. This reflects the heavy start up costs of mapping and technical assistance necessary to bring 10,000 communities into the regular program. This also reflects the prevalence of subsidized flat rates in preference to actuarial rates based on the actual risk at particular locations. The Flood Insurance Program is nevertheless a bargain as compared with other federal investments. For instance, the GAO in its report on the "water project construction backlog" of January 26, 1983 reports that the Corps of Engineers in Bureau Reclamation have approximately 934 authorized water projects needing about

60 billion dollars to complete construction. It is likely that detailed analysis could demonstrate that the 1.5 billion devoted to the Flood Insurance Program has resulted in continuing benefits that will far outweigh its costs. Furthermore, FEMA is continuing to study and adjust its actuarial weight structure so as to approach its objective of making the National Flood Insurance Program fiscally self-sufficient.

Having now stated my opinion that the National Flood Insurance Program overall is having a favorable and beneficial impact on the level of flood losses in the United States, I would like now to turn to certain problems which may be discussed in further detail.

Whither the Emergency Program?

Considerable discussion is currently being devoted to the question of what should be done about the remaining 7,000 communities in the emergency program. Most of these communities are small rural municipalities or outlying counties with few flood insurance policies and little program activity. One issue is whether FEMA should conduct detailed flood studies in these generally extensive and sparsely settled areas. A second issue is whether these communities should be transferred to the regular program in the absence of detailed studies and thereby enjoy the full benefits of the NFIP. It is my understanding that the General Accounting Office is recommending that flood insurance studies be suspended for these communities and that they be converted to regular program status forthwith. FEMA, on the other hand, would like to continue detailed mapping for at least some of these communities and convert them gradually over the next three years.

In my opinion, it is unnecessary to conduct detailed engineering studies in most of the remaining 7,000 emergency program communities. It is far more important to use available study money for re-study of regular program communities where landuse changes are rendering earlier maps obsolete. According to a study in which I participated with the National Academy of Science, expedient methods could be used for large-scale mapping of hazard areas in outlying communities which would be administratively efficient, fiscally economical, and legally defensible. However I agree with FEMA that these communities should not be converted to regular program status arbitrarily. Eighty percent of the communities now in the regular program have earned that status through adoption of floodplain management regulations. It has become a matter of distinction for a community to participate in the regular program. This status should not be diluted by converting several thousand communities with little effort on their parts. Furthermore, I would oppose the extention of regular program levels of coverage to communi ties which have not adopted full-scale flooplain management requirements.

As a middle ground, I would suggest that a special category might be established for communities which are not expected to have much flood insurance activity or development in flood hazard areas. Existing development could continue to qualify for emergency program levels of coverage but new development would receive no insurance at all in flood hazard areas.

This should not be construed to deny federally-related financing for such construction however. Upon evidence of significant development potential in a community it should be subject to detailed study and converted to full regular program status.

Enforcement of Local Regulations

A crucial issue for the National Flood Insurance Program in coming years is to ensure that communities in fact enforce their regular program regulations. This requires periodic monitoring of local activity and administrative practices by outside authorities. Through its program entitled Community Assistance and Program Evaluation (CAPE), FEMA intends to evaluate every participating community at least once every five years however it has not generally met this goal to date. Dwindling field staff resources in the face of growing numbers of communities in program activity threaten to make the CAPE program totally ineffective.

I would suggest a two-fold approach to this program. First, FEMA should refrain from diverting the time and energy of its floodplain management staff members to other areas of activity. FEMA's regional floodplain staff have been few in number but diligent and highly motivated. It is undesirable to dissipate their talents upon unrelated matters which could better be handled by other staff.

A second approach would be in some cases for FEMA to enter into contracts with state government or regional entities such as the Delaware River Basin Commission to conduct monitoring and enforcement of local compliance. This would have the advantage of strengthening the floodplain activities of the state or regional agency in question, and also would remove some of the workload from the FEMA regional offices.

Non-Metropolitan Areas

A surprising proportion of NFIP activity occurs outside of standard metropolitan statistical areas. As of April 8, 1981, 49% of regular program communities were non-metropolitan as were 76% of emergency program communities. Non-metropolitan areas accounted for 30% of the total number of flood insurance policies, 23% of total coverage, 27% of all claims and 20% of the total amount of claims by that date.

These figures suggest that non-metropolitan areas including small cities and rural counties account for a significant fraction of NFIP activity. Many kinds of flooding are involved, e.g., shallow agricultural flooding in the Red River Valley of the north, flash flooding in Appalachia and the Rocky Mountains, alluvial fan flooding in the west, coastal flooding along Barrier Islands, and tributary overflow in the Mississippi Valley. FEMA must therefore be flexible and sensitive to regional variations in flooding conditions and types of damage resulting therefrom. This involves complex methods of mapping methodology, actuarial rate setting and drafting of standards for regulations. With the program now widely in effect and generally accepted, FEMA must turn its efforts increasingly to "fine tuning"

of its requirements and study methodology for regions with differing circumstances. As with monitoring and enforcement, FEMA should wherever possible contract with state or regional agencies to perform special studies so as to gain the benefit of local knowledge and regional experience.

Coastal Areas

Coastal flood hazards have been the achilles heel of the National Flood Program. Coastal areas account for a disproportionate share of property at risk and program activity. Ninety barrier island communities alone account for about 5% of the total number of flood insurance policies and 7% of total coverage. The average number of policies in these ninety communities is 1,168 as compared with 106 in other participating communities. It is well known that coastal areas of the Gulf and Southeast Atlantic have been spared devastating hurricanes for some years. Potential losses and flood insurance liability in these areas is astronomic.

FEMA has sought to improve the validity of its coastal studies and maps, particular in "coastal high hazard areas" facing the open ocean. Wave heights have been incorporated into recent studies and actuarial rates have been adjusted to be more realistic.

Meanwhile Congres has adopted the Coastal Barrier Resources Act of 1982 (PL 97-348) which prohibits new flood insurance coverage and other federal benefits to designated "undeveloped" coastal barriers. This act sensibly recognizes that federal investment has indirectly sponsored much coastal development in hazardous areas, thereby undermining the objectives of the National Flood Insurance Program and other disaster mitigation policies. However, the act will effectively increase pressure for development in areas outside of its protection, namely so called "developed" coastal barriers and other coastal areas which still have much natural open land. Flood insurance continues to be available for new construction in such areas, even in the coastal high-hazard area zone. I would strongly recommend that flood insurance be denied for new development in the coastal high hazard area and be carefully evaluated in other coastal areas.

In closing, I would like to reiterate my generally favorable impression of the National Flood Insurance Program and the efforts of FEMA to promote flood hazard mitigation at all levels of government. These efforts must continue. Funding must be sufficient to allow necessary staff expansion to cope with the increasing workload and scope of the program. In addition, the mapping program, and especially re-studies of earlier maps, should be continued at a reasonable level. Communities currently in the emergency program should not be converted directly to the regular program but should be put into a holding status pending further consideration. I appreciate this opportunity to comment on the program and would be happy to respond to questions.

Senator HECHT. Thank you very much.

Ms. Whilden, could you explain what sort of resources are available through the existing data study?

Ms. WHILDEN. Well, many States generate information. There are regional commissions that have generated information and some local communities generate information, but unless they are officially added onto flood insurance rate maps they are not considered for insurance purposes.

MAKE BETTER USE OF FLOOD HAZARD MAPS

Senator HECHT. Couldn't we make better use of existing data to make flood hazard boundary maps comparable to flood insurance rate maps?

Ms. WHILDEN. Absolutely; about 20 percent.

Senator HECHT. Thank you. The General Accounting Office has testified that as many as half of the areas that remain unmapped are not undergoing any development. If this is true, wouldn't this minimize the loss of flood plain management if the program were transferred from the emergency to the regular program?

Ms. WHILDEN. If that's the case, yes, of course. In some communities they have taken care of flood plain management with setback regulations, for example, but I guess another big problem with my perception of the GAO report was that not enough research went into it to document some of those figures and I know FEMA is planning to do such a research project.

Senator HECHT. Thank you. You have testified that if the General Accounting Office's proposal was modified to insure that future construction would not be subject to flood hazards you would reconsider your stand against this proposal. How could that be achieved?

Ms. WHILDEN. Well, there again, my perception was that the GAO proposal did not include specifics on what level of regulations these communities would be required to regulate. For example, in the State of New Jersey there are over 85 communities converted and I think they are regulated to what is known as the B level, which in essence is communities use the best available data, and if they can't find it, that's OK; just do the best they can. There are problems with that vagueness because we don't know by what standards these communities are going to be required to regulate them.

Senator HECHT. Thank you. Mr. Platt, you mentioned your work with the National Academy of Sciences study which found that expedient methods could be used for mapping which would be more efficient and economical. Will you elaborate on that?

Mr. PLATT. Yes, sir. Only to the extent of the legal aspects which is my particular concern on that committee. Legal research was conducted by myself and also by consultants to the Academy and to FEMA which indicated that courts are willing to uphold regulations based on studies which use less than the most sophisticated or the most expensive methodology available. So that there are a variety of techniques, I understand, based on remote sensing photogrammetry and other kinds of methods which are available for potential use in the program, and I would refer to colleagues in perhaps the University of Maryland department of geography or the

remote sensing center at my university in order to give a more detailed answer on the techniques themselves.

Senator HECHT. I appreciate both of you coming here today, and, because we are running late and in the absence of my colleagues, which I think have some questions to ask you for the record, I will also be submitting additional questions to you.

Could we have the third and final panel, please. Thank you very much for appearing before us. I have the order as the Honorable James Corcoran starting off.

STATEMENT OF JAMES CORCORAN, SUPERINTENDENT, NEW YORK STATE INSURANCE DEPARTMENT

Mr. CORCORAN. Thank you, Senator.

[The complete statement follows:]

STATEMENT OF JAMES CORCORAN, SUPERINTENDENT, NEW YORK STATE INSURANCE DEPARTMENT

Good Morning, my name is James Corcoran, and I am the Superintendent of the New York State Insurance Department. I wish to thank Senator Hecht and the members of the Insurance Oversight Subcommittee for the opportunity to appear before this committee concerning the Federal Crime Insurance Program.

The Administration has determined that the Federal Crime Insurance Program should not be continued after its currently scheduled expiration. On behalf of Governor Cuomo and the people of the State of New York, we urge the members of this Committee and the Congress to extend this vitally needed program.

As you know, the Federal Crime Insurance Program was created in 1970 and became effective on August 1, 1971. The specific purpose of the program was, and is, to provide crime insurance at an affordable price in any State that has a crime insurance availability problem and does not have an appropriate state program to provide a solution.

Clearly, one would expect that the utilization of such a program would be greatest in the large Urban States which elected to participate. It is, therefore, not so surprising that this program's utilization has been limited to a few states since this was the program's original intent. However, it is important to note that the extensive utilization of the program in New York is primarily due to the efforts by the N.Y. State Insurance Department to publicize the existence of the program. The "Consumers' Shopping Guide" published by the N.Y. State Department of Insurance, not only sets forth the general provisions of the Federal Crime Insurance Program but also clearly sets forth where additional information can be obtained. I, therefore, have no doubt that if other states were to adopt a program, similar to New York, of publicizing the benefits of Federal Crime insurance to the consumer, that you would see a higher utilization of the program in other states.

The Administration's desire to terminate the Progam appears to be based in great part on the fact that three States, New York, Pennsylvania and Florida account for most of the utilization with over 70 percent of the policies written under the program.

If concentration of utilization of a Program were to be considered a valid criteria for termination of the Progam, than that same criteria should be applied to other Federal Programs as well.

It should be noted that under the Federal Flood Insurance Program, three states, Florida, Louisiana and Texas accounted for 66 percent of the policies in force as of December 31, 1981. However, neither I, nor anyone else, would seriously suggest that such a necessary Federal Program be terminated merely because its utilization was concentrated in a small number of geographic areas.

On April 15, 1982 the U.S. General Accounting Office issued a report entitled "The Federal Crime Insurance Program: An Overview." This highly subjective report contained several misleading statements concerning the Program and its use in New York,

Concerning the question of affordability, the report, referring to the $60 residential premium then in effect stated:

"If a $60 premium charged by the Federal program is affordable, is an $85 or $100 private insurance premium not affordable?"

The statement clearly implies that the cost of private insurance would only be marginally higher than the insurance available under the Federal Crime Program. This is definitely not true.

As a result of program changes implemented on June 1, 1982, the current premium for residential policy is $120 for $10,000 coverage, the maximum amount available. The annual premium for a residential burglary and theft policy in the amount of $10,000 obtained from a licensed private insurer for a person living in Brooklyn would be $220 based upon rates filed by the Insurance Services Office, a major rating organization. However, this rate is largely unused by the insurance industry. ISO has informed us that in 1980 only $11,900 in premiums was written in Brooklyn using their rates. This accounts for approximately only 75 policies. Most companies would be unwilling to insure these individuals even at that rate, and would require the insureds to consent to a higher rate as provided by Section 185(3) of the N.Y. Insurance Law.

The number of policies written under the Federal Crime Program has been steadily decreasing both program wide and in New York. Part of this decrease may be attributable to the program changes that have taken place over the past three years, which have increased premiums and deductibles and tightened up the claims handling process. However, part of this decrease may also be attributable to the renovation and reconstruction of certain areas of New York City, which have been aided by the existence of the Federal Crime Program.

There are many neighborhoods in New York which participated in the Program when it was introduced and the availability of crime insurance provided the element of stability to allow businesses to invest, and encouraged residents to remain in the neighborhood. This phenomenon together with the increase of crime in the suburbs is not peculiar to New York State. It is a national problem.

The situation concerning the 9,000 commercial insureds in New York is even worse. Although the premiums for commercial risks are comparable between the Federal Crime Program and the private insurance industry, these commercial risks, for the most part, could not obtain insurance in the voluntary market.

These businesses are located in areas of New York City which have a high incidence of burglary and theft. The claim experience of these commercial risks makes them uninsurable in the eyes of private insurers, and yet, small business is the very life blood of these communities. It is these businesses which provide jobs, services and tax dollars in communities where such benefits are most needed. If these small businesses are unable to obtain the benefits of the Federal Crime Insurance Program, many would be forced to close their doors with the predictable result of greater expense to local, state and the federal government due to lost taxes and increased need for public assistance.

Like all of you, I look forward to the day when the need for a federally subsidized program of crime insurance will no longer exist. However, we are at present, still faced with a "central market availability situation for crime insurance" which can only be addressed by the Federal Crime Insurance Program. It should, therefore, be continued.

ROOM FOR IMPROVEMENT ON PROGRAM

Mr. CORCORAN. After reviewing my notes and making a few other observations on the program, there is room for improvement. I do see in certain sections that there is not a requirement in the program that the individual person include financial need or are able to afford private insurance carriers and also that they don't have to prove they are unable to obtain it at commercial rates. So there are changes I can see being made. Many people can afford the insurance, but there are many people who cannot afford AAA premiums which we see in residential insurance. The figures I have seen from my department has shown that the premium would triple if the program is eliminated. Many commercial lines would be available.

Senator HECHT. Let's hear from Mr. Bernstein.

STATEMENT OF GEORGE K. BERNSTEIN, AMERICAN INSURANCE ASSOCIATION, ACCOMPANIED BY PENNY FARTHING

Mr. BERNSTEIN. Thank you, Mr. Chairman. Appearing with me today is Penny Farthing, senior counsel of the American Insurance Association, who will answer questions with me.

[The complete statement follows:]

TESTIMONY OF GEORGE K. BERNSTEIN

On Behalf Of

THE AMERICAN INSURANCE ASSOCIATION

The American Insurance Association (AIA), comprised of 165 property/casualty insurers, has been a leading proponent and supporter of the National Flood Insurance Program and the Urban Property Protection and Reinsurance Program, both of which were enacted in 1968. Since the passage of the Federal Crime Insurance Act in 1970, AIA has also supported that program. AIA urges continuation of all three programs.

National Flood Insurance Program

The National Flood Insurance Program was enacted because broadly based, self-supporting private insurance against flood losses was impossible. Congress recognized that the flood hazard is essentially uninsurable. Floods combine the elements of low frequency of occurrence and high severity of loss that are inconsistent with a sound insurance program because of the inability to spread the risk and the resultant extreme adverse selection.

Congress appreciated these problems, and undertook the development of the National Flood Insurance Program with no illusions. The 1968 Act was a trade off under which the federal government would compensate victims of flood losses who had already located in flood prone areas. In return, with respect to new construction in areas where the flood hazard was known and documented, federal flood insurance would be available only if proper locational and construction decisions were made by communities and individuals.

Congress also recognized that the cost of flood coverage would be equally prohibitive whether it was sold by the federal government or private insurers, and the Act provided heavily subsidized federal premium rates for existing construction.

Subsidies were at the heart of the program. If subsidies had not been necessary, neither would a federal r Without subsidies, even a federal program would have been failure.

Nevertheless, the Act directed that after appropriate information on the flood hazard had been provided to local communities, premium rates for new construction would be set on an actuarial rather than a subsidized basis. Congress so structured the Act for several reasons: no subsidy was intended for development that disregarded documented flood hazards; actuarial rates for new construction would create an economic incentive for safer development; and if proper construction practices were implemented, new structures would be sufficiently safe from flooding to permit premium rates that were affordable without a subsidy.

As Federal Insurance Administrator, I testified before this Committee, the House authorization Committee and the Appropriation Committees of both houses over a period of five and one-half years. Each time, I advised the committees that the flood insurance program was insurance in name only. Despite the fact that we know far more about flood damage and its mitigation than about such other hazards as earthquake, even

the setting of actuarial flood insurance rates is far from a science. The unpredictability of wind and wave elements, the low frequency, high severity nature of the risk and the need to use such estimates as the "100 year flood" as a standard for both ratemaking and hazard mitigation, do not permit the precision expected in an insurance program.

Accordingly, massive losses and high costs to the Treasury were expected for many years until the location and quality of, and premiums for, new construction would overtake the risk of structures currently exposed to severe flood damage.

Unless the hazard mitigation requirements of the Act are strictly enforced, these costs would be unjustified, and relatively inexpensive federally subsidized premiums would actually encourage irresponsible construction in flood prone areas. The result might be greater losses than would have occurred without a federal flood insurance program.

It should come as no surprise that the program has paid well over a billion dollars in claims, which, even without the significant additional expenses of engineering, mapping and the administration of the program, far exceed premium income. These costs constitute an investment in the long term goals of safer construction and wiser use of flood prone areas, and reflect the underlying premise of the program that eventually the cost to taxpayers would be less under a balanced flood insurance program that under the haphazard, ad hoc approach of disaster relief.

Whether this investment is paying off is a question which Congress must assess in determining whether to continue the commitment of taxpayer dollars to the subsidization of flood insurance. The 1973 Flood Hazard Protection Act, mandates that federal flood insurance be purchased for any structure in a high hazard area if the community has joined the program and if a mortgage is issued by a federally insured lending institution. Under these requirements, the current $100 billion of federal exposure under this program will continue to grow. Only if the program is well managed and the hazard mitigation provisions are wisely and earnestly enforced will the federal investment be justified.

Although the Federal Insurance Administration (FIA) has affirmed its commitment to the hazard mitigation aspects of the program, there are very real pressures from private, local, state and federal sources who would prefer that enforcement take place in someone else's community or not at all. Unless the Congress and the Administration withstand these pressures, the goals of the program will not be achieved.

The lastest manifestation of such pressures is the introduction of S. 460 and H.R. 1885, which would amend the 1968 Act to permit the sale of federal flood insurance even in communities that fail to adopt "adequate land use and control measures" required by the Act.

By authorizing the sale of insurance to individuals despite the failure of the community to enact the required land use and control measures, the proposals would remove the

primary incentive for enactment of such essential measures. It is only pressure from individual homeowners and businesses, seeking the availability of flood insurance, that overcomes the countervailing pressure from developers who resist the enactment of land use and control measures and attempt to continue less expensive but more hazardous construction in flood prone areas by keeping the community out of the program.

FIA has indicated its desire that private insurers again play a role in the flood insurance program. Until 1978, insurance companies bore a share of the underwriting risk of the program.* In addition, in return for servicing fees, private insurers issued policies and handled claims for the FIA. Since 1978, the federal government has taken over both risk sharing and servicing of the program, with the latter function contracted out to a non-insurer.

Inasmuch as one of the goals of the original flood insurance legislation was that the federal role would gradually diminish and be replaced by an increasing private insurance responsibility, the AIA welcomes the desire by the FIA to explore renewed private insurer involvement. The AIA is prepared to make its expertise and that of its companies available to FIA.

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* The industry share was roughly proportionate to the ratio of the premium dollars actually realized through subsidized rates to the actuarial rate. Insurers also could purchase reinsurance from the federal government against excess losses.

The Federal Insurance Administrator has recognized that a private risk bearing role is premature, and has stated that he does not seek such an industry commitment at this time. The AIA concurs with the Administrator.

Whether private risk sharing can be reconstituted at some future date depends on an assessment of the fiscal and political climate to determine if the insurance program is operating on a sound basis, and if the insurance industry can work out a cooperative arrangement through which its interests and those of the public are adequately protected.

It has been suggested by the FIA that even in the absence of a private risk bearing role, insurers may be interested in acting in an administrative or servicing capacity to the National Flood Insurance Program, or by issuing the federal coverage in the form of private policies. These alternatives are currently being explored and, will, no doubt, be pursued further after FIA executes a new servicing contract, effective September 30, 1983.

Regardless of the extent to which the private insurance industry may participate in the federal flood insurance program, and even if there are substantial program changes, no one should be under any illusion that the need for substantial federal subsidies will disappear.

Given the vast majority of "existing" structures that will continue to populate the program for years to come, and the Congressional mandate that such properties not be required to pay more than an "amount, consistent with the objective of

making flood insurance available where necessary at reasonable rates so as to encourage prospective insureds to purchase such insurance and with the purposes of this chapter,"* premium income will be inadequate to support the program for the foreseeable future. Accordingly, the reasons why the private insurance industry was unable to provide flood insurance on a broad, self-sufficient basis, and why Congress enacted a subsidized program in the first place, continue to exist.

Urban Property Protection and Reinsurance Program

The riot reinsurance program was enacted as a response by Congress to the unavailability of property insurance in central city areas following the urban riots in the mid to late 1960s. Congress recognized that insurance availability problems would continue if private insurers were concerned about concentration of urban property exposures and uncertain of the availability of private reinsurance.

The legislation established conditions that were to be met before private insurers were permitted to purchase the federal reinsurance. These conditions assured residents and businessmen of basic property insurance coverage from private insurers through state regulated FAIR plans, but the 1968 Act did not interfere with the state ratemaking process or the prerogatives of individual insurers to exercise sound underwriting judgments. The American Insurance Association

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* 42 USC §4015(b)(2)

not only enthusiastically supported the 1968 legislation, but its companies were in the forefront in purchasing federal riot reinsurance.

Through the FAIR plans and individually, insurers have made significant amounts of insurance available in urban areas. Since inception of the program, more than three million FAIR plan policies have been issued to residents and businessmen in the 28 states with FAIR plans. $2 billion in claims have been paid to FAIR plan insureds. FAIR plans have paid out more than $500 million more than they have received in premiums and investment income.

Unlike the federal flood insurance program, there has never been a subsidy of federal riot reinsurance premiums. Rates were set on the basis of the actual exposure of the federal government. From the beginning, the federal reinsurance rate took into consideration the existence of a state obligation to share in the federal losses, as well as the right of the FIA to assess private insurers (in addition to their premium payments), for a certain level of federal losses.

After payment of all losses and expenses, the government realized a surplus of more than $120 million trom the sale of such coverage. Private insurers more than paid full price for the security of federal reinsurance.

Currently, however, only 12 reinsurance contracts have been entered into with FIA by private insurers, a fraction of the number in past years. Despite the fact that since the

program began, AIA companies were the leading purchasers of the federal coverage, none of the 165 AIA companies has indicated that it purchased it this year. The primary reason for this drop in industry interest in federal reinsurance is the tenfold rate increase imposed by FIA beginning with the 1982 contract year. As the AIA predicted in its 1981 testimony before this Committee, there is little interest in a program with unrealistically high premium rates.

At 25 cents per $100 of coverage, the FIA rate is grossly excessive, has no relation to actual past or anticipated future riot losses, and few insurers are willing to pay such a price when private riot reinsurance is available at substantially lower cost. In fact, FIA does not even claim that the 25 cent rate is needed to cover expected riot losses, but has set that rate to discourage participation in the program. If an alternative intent of FIA was to produce a surplus to fund the losses generated by the entirely separate Federal Crime Insurance Program, it has not succeeded, as the 1000% rate increase has scared off more insurers than it has attracted additional premiums.

As private market riot reinsurance is currently available at reasonable cost, and as insurers believe that they are better prepared today than they were in 1968 to respond in an orderly fashion following an outbreak of serious rioting, few companies can be expected to purchase the high priced federal coverage.

Nevertheless, over the years, the federal riot reinsurance program has succeeded in encouraging private

insurers to make essential insurance available in urban areas. Despite the drop in the number of insurers that are purchasing the federal coverage, the AIA believes that the continued existence of the program is necessary.

Some insurers, particularly smaller ones, still purchase federal riot reinsurance, and the AIA would not deny them the opportunity to retain this security. Moreover, if circumstances change, and if federal riot reinsruance again becomes critical, as it did in 1968, it would seem unwise to terminate the program only to have to seek new legislation to resurrect it.

The knowledge that the program exists and that federal riot reinsurance is potentially available is a significant factor in keeping insurance markets open in our urban areas.

Under the existing legislation, no insurer is required to purchase the federal coverage, and its availability is unlikely to impose financial costs on any insurer that chooses to obtain its riot reinsurance only in the private market. Those insurers that oppose the program are free to ignore it without penalty or burden.

Furthermore, the cost to the federal government of retaining the program is more than covered by the premium income received. Since inception in 1968, total program expenses have been only $4 million. Against these costs, the government has netted more than $120 million over the life of the program, even after payment of all reinsured losses. Even in the period ending October 1982, the government took in $676 thousand in riot reinsurance premiums, had no losses to pay and spent only $111 thousand in expenses.

The advantages of continuing the federal riot reinsruance program impel the AIA to urge extension by the Congress.

Federal Crime Insurance

In enacting the Federal Crime Insurance Program in 1970, Congress acknowledged that crime losses in certain urban areas were as uninsurable as those from floods.

The 1970 Federal Insurance Administration report, which preceded the Congressional action, found that:

> "The choices we have as a society are not easy. We must decide not only whether we want to save our urban areas, but also whether we are willing to pay the price. This report demonstrates that traditional insurance approaches are inappropriate to the problem of crime losses in the areas most seriously affected. It is impossible for the residents of these areas to bear the full financial burden of either their uninsured losses or their own insurance costs as traditionally determined under the rating laws of the several States. If we are to compensate these residents for crime losses, the cost of this compensation must in part be borne by others."*

Following issuance of that report, Congress chose not to rely on state solutions to the problem, and developed a direct federal program to compensate crime losses.

As with federal flood insurance, there were no illusions that the program would be self-sustaining, and Congress decreed that premiums were to be "affordable", rather than actuarially sound, so that residents and businessmen in high crime areas could purchase the coverage. While it was intended

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* Report on Availability of Crime Insurance & Surety Bonds in Urban Areas, Federal Insurance Administration, U. S. Department of Housing and Urban Development, 1970, p. 3.

that in the early years of the program costs would be advanced from the riot reinsurance surplus in the National Insurance Development Fund (NIDF), it was understood that appropriations would ultimately be required. However, no such appropriations have been made and crime insurance losses have wiped out the $120 million surplus of the NIDF.

Despite extensive protective device requirements, which private insurers would find difficult, if not impossible, to enforce, the federal government has paid more than $3 in losses and expenses for every dollar of premium income--about $230 million has been expended against approximately $70 million in premium income. Even with more extensive protective requirements and greater premium income in the last year, the program was still paying out $2.60 for each dollar taken in as of October 1982.

Such losses are consistent with the Congressional intent in enacting a program that was not true "insurance", but was a response to a social problem of such scope in certain states that private solutions were unlikely.

Nothing has changed in the last twelve years to bring the reasoning behind the 1970 Act into question. Excessive crime losses, concentrated in heavily populated urban areas would still require insurance premiums that, without a subsidy, would prove prohibitive, regardless of whether such coverage was sold by the federal government or by private insurers.

The federal government may choose to reevaluate its decision that the social problem of crime losses should be

addressed by a government program, or that on a relative scale of values, crime insurance ranks sufficiently high to justify the costs that must ultimately be borne by the Treasury and the taxpayers. But the actual experience of the Federal Crime Insurance Program is devastating proof that compensation for losses from crime cannot be accomplished without a subsidy.

Recent premium increases have somewhat reduced program losses. Neither such increases, however, nor increased deductibles nor stepped up enforcement of protective requirements will alter the basic need for subsidies in multiples of the premiums charged.

Premium increases may well have been necessary, but continued premium increases of similar magnitude may tip the balance of an appropriate subsidy. When premiums are raised so high as to discourage purchase of the federal coverage, rates may no longer be "affordable", and the demise of the program may be a self-fulfilling prophesy.

The recent drop in coverage probably reflects this phenomenon. At the same time, the failure to market the program, by apprising those most in need of its coverage, must also contribute to reduced coverage. Again, a proper balance must be struck between pushing a program and advising those for whose benefit it was created that it exists.

Undoubtedly, there are states in the Federal Crime Insurance Program where both number of insureds and losses are minimal enough for coverage to be provided through private or state mechanisms. However, in high crime areas where

there is significant demand for the coverage, the scope of the exposure precludes private, non-subsidized solutions.

Private insurers must base their rates on actual experience, and the private insurance mechanism is not structured to provide the extensive subsidies required by a social insurance program. As long as government desires an "affordable" premium structure to insure against a severe social problem, the federal crime insurance program is the most appropriate method for providing crime insurance to high risk insureds.

The federal subsidy for crime insurance, is no different in principle than that for federal flood insurance--and the cost of crime insurance is a fraction of the cost of flood insurance to the taxpayer.

Just as flood insurance benefits some areas of the country more than others, crime insurance is no less significant to the economic viability of many urban areas. Certainly, the importance of Federal Crime Insurance in the structure of the proposed enterprise zones cannot be minimized.

The American Insurance Association has supported the federal flood, riot and crime insurance programs since their inception. Whatever approach is taken on the continuation of these programs, the AIA and its companies will continue to work with the Congress and the Administration to help make essential insurance coverages available.

STATEMENT TO: Subcommittee on Insurance, Senate Committee on Banking, Housing and Urban Affairs

BY: Professional Insurance Agents of New York State, Inc.

RE: CONTINUED AUTHORIZATION OF THE FEDERAL CRIME INSURANCE PROGRAM

SUBMITTED ON: April 8, 1983

As an association representing nearly 18,000 people who are employed by approximately 2500 member insurance agencies and brokerages, the Professional Insurance Agents of New York State, Inc. (PIANY) respectfully requests that the following statement be included in the record of the hearing on reauthorization of the federal crime, flood and riot reinsurance programs, held April 8, 1983.

On behalf of our members and the customers they serve, we urge your committee to recommend a continuation of the Federal Crime Insurance Program for an additional two-year period.

When this program was originally established, its purpose was to provide a market for crime protection to businesses and householders who would otherwise be unable to obtain it. The need for this program continues unchanged. Approximately 27,000 families and 9,500 business owners in our state depend on the program for their crime insurance coverage.

We speak from first-hand knowledge when we assure your committee that, whatever conditions may prevail elsewhere, there is no private market willing to furnish this coverage in certain areas of our state. If the federal program were suddenly withdrawn, the impact would be severe for the homeowners, tenants and particularly the small business owners who bravely carry on in high-crime areas. The very viability of these businesses and the precarious neighborhoods which depend on them is threatened by the loss of access to crime insurance.

In recognition of the serious crisis which would be posed by the possible discontinuation of the program as of May 20, 1983, PIANY has called for a meeting of the insurance industry, the New York State Insurance Department, and other producer groups to be held April 15, 1983 in New York City. However, we are not optimistic that any resolution, much less a satisfactory solution, can be worked out under crisis conditions.

For this reason, we again urge your committee to provide the stability of a two-year extension of the Federal Crime Insurance Program. Under these conditions, perhaps long-term answers can be found to the dilemma of providing this essential insurance coverage at an affordable cost to those citizens who need it most.

Respectfully submitted,

Daniel J. Kraft

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Senator HECHT. Thank you.
Mr. Jones.

STATEMENT OF JAMES E. JONES, JR., GOVERNMENT AFFAIRS REPRESENTATIVE, ALLIANCE OF AMERICAN INSURERS

[The complete statement follows:]

STATEMENT OF THE

ALLIANCE OF AMERICAN INSURERS

AND

NATIONAL ASSOCIATION OF MUTUAL INSURANCE COMPANIES

Mr. Chairman and members of the Subcommittee, I am James E. Jones, Jr., Government Affairs Representative for the Alliance of American Insurers. I have been asked today also to speak on behalf of the National Association of Mutual Insurance Companies (NAMIC). NAMIC and the Alliance together represent in excess of 1,350 large and small property and casualty insurance companies providing insurance protection throughout the fifty states and the District of Columbia.

We very much appreciate the opportunity to present our views on the federal property insurance programs administered by the Federal Insurance Administration.

A. The Urban Property Protection and Reinsurance Act of 1968 (Federal Riot Reinsurance Program)

Mr. Chairman, we believe that this federal program has outlived its usefulness and we urge that it not be extended beyond September 30, 1983. The Urban Property Protection and Reinsurance Act of 1968 authorized the federal government to sell riot reinsurance to private insurance companies following the urban riots of the mid 1960's. The Act was needed to assure that essential property insurance would remain available in urban centers following those civil disorders. The program was a major recommendation of a National Advisory Panel established by President Johnson in 1967 to study the problems of insurance availability in the riot affected areas of our cities. The

Commission concluded that a joint government private industry program was needed. The Alliance, at that time, was strongly supportive of the Panel's decision.

The Federal Riot Reinsurance Program has now been in effect for 15 years. The Program has been a highly successful joint venture. For ten of those 15 years it was also a very profitable endeavor for the federal government. Premiums collected by the government from the Riot Reinsurance Program at one time substantially exceeded losses. This enabled the federal government to establish large reserves -- approximately $140 million which, in turn, were used to subsidize the federal crime insurance program losses. As a result of this subsidization, however, these reserves have now been depleted. In fact, today, the federal government is no longer collecting enough premiums from the insurance companies to cover even the losses arising out of riot related incidents.

The National Advisory Panel did not limit its recommendations to the establishment of a Federal Riot Reinsurance Program. It also proposed that in return for this federal program, the states should individually establish insurance mechanisms which would assure property owners of the availability of insurance protection. Insurers participation in those individual programs was to be a requirement for any one insurer being allowed to purchase the federal reinsurance. The Alliance also was supportive of this proposal and affirmatively worked with the states for its implementation.

As a result, separately, many jurisdictions (28) established pooling arrangements known as FAIR (Fair Access to Insurance Requirements) Plans. Properties which could not be insured in the voluntary markets would be

insured by these FAIR Plans. Insurance Companies providing insurance in a jurisdiction in which a FAIR Plan had been established would share in the losses and earnings generated by FAIR Plan insurance coverage.

FAIR Plans have also been highly successful. They have provided the basic property insurance necessary to rebuild our cities. They have also become an intricate part of the insurance market network. Some of these plans today extend considerably beyond just providing essential insurance. They are now offering to urban residents a choice of insurance coverages similar to that available in the voluntary market. In fact, the plans in Illinois, Massachusetts, Rhode Island, Wisconsin and Ohio now issue homeowner package policies.

Although these plans have achieved their objectives to provide availability of insurance coverage in our cities, they have been costly for our member companies. Over the past five years, losses incurred have exceeded premiums collected by $286 million (1977-1981).

The Federal Riot Reinsurance Program was essential to the establishment of these FAIR Plans. Today, however, market conditions have changed considerably. Private reinsurance coverage is available to cover losses resulting from possible urban riot or civil commotion. There is ample private reinsurance capacity and primary insurers today have looked to the private reinsurance system for its urban riot and civil commotion reinsurance needs.

The figures speak for themselves. At one time, 474 private insurers were purchasing riot reinsurance coverage from the federal government for $35 millions of dollars in annual premiums. Today, only 17 companies paying annually approximately $130,000 of premium participate in this federal program.

The riot reinsurance program no longer meets a public need. Its elimination will not have an adverse effect on the general availability of property insurance in urban areas. State FAIR Plans have become an intricate part of the insurance marketing system. The termination of the federal program will not affect these FAIR Plans.

As a matter of fact, all of the FAIR Plan states except for Georgia and Pennsylvania have adopted legislation to assure the continuation of the Plans independently of the availability of the Federal Riot Reinsurance Program. I am assured that if the federal program is not reauthorized, both Georgia and Pennsylvania will enact legislation to provide for the continuation of their state FAIR Plans.

Those who allege that the Federal Riot Reinsurance Program is needed to assure the continued existence of FAIR Plans, just do not have history on their side. There are today nine states (California, Indiana, Iowa, Kansas, Kentucky, Louisiana, New York, Ohio and Oregon) whose FAIR Plans no longer meet federal regulatory requirements. As a result, insurers operating in those states may not purchase federal riot reinsurance to cover riot or civil commotion property losses occurring in those states. Yet, there has been no attempt whatsoever to discontinue the FAIR Plans in those states.

The Subcommittee should be aware that when the federal riot reinsurance reserve fund became depleted, the Federal Insurance Administrator, on October 1, 1981, increased the riot reinsurance premium from 2½¢ per $100 to 25¢ per $100. This amount generally exceeds rates charged by private reinsurers and, is another reason for the dramatic shift by private insurers away from the federal insurance program.

This Administration has made it clear that it wants to terminate those federal programs which have become redundant and whose purposes can best be accomplished through reliance on the private sector. In our opinion, the riot reinsurance program is an outstanding example of a federal program which can be terminated without loss of services or benefits to anyone. The only justification for federal involvement in providing insurance protection is when such coverage is essential and is not readily available in the private insurance market. These conditions no longer exist today.

Mr. Chairman, our members have considered the present depressed state of the economy. They are aware that predictions have been made that these conditions might well lead to renewed civil disturbances. They remain firm, however, in their conviction that the Federal Riot Reinsurance Program should be discontinued.

We know that it has been and probably will continue to be argued that this program is needed to insure the availability of insurance in our urban centers. Those making such assertions just do not have the facts. One only has to look at what happened in Florida following the series of riots over the past three years in Miami. Florida does not have a FAIR Plan and therefore is not eligible to participate in the federal reinsurance program. Yet, insurance availability is not a problem there in spite of the fact that the insurance industry sustained in excess of $60 million losses during the 1980 disturbances alone.

For these reasons, Mr. Chairman, we urge that the Federal Riot Reinsurance Program no longer be authorized after September 30, 1983. There is declining participation in the program by private insurers. This trend will continue. The discontinuance of the program will not affect services or insurance availability. Private reinsurers are providing primary insurers with adequate

reinsurance at cost less than those established by the federal government. The Federal Riot Reinsurance Program is today operating at a loss and is a drag on the federal treasury. It is no longer needed. It serves no purpose. It should be terminated.

B. Federal Crime Insurance Program

The Federal Crime Insurance Program was established under the 1968 Urban Property Protection and Reinsurance Act. The act authorizes the federal government, as an insurer, to provide crime insurance at an affordable price in any state that has a critical crime insurance availability problem and does not have an appropriate state program to provide a solution. The Crime Insurance Program became effective August 1, 1971.

The Alliance and NAMIC support the Administration's position that the program should not be authorized beyond September 30, 1983.

The Federal Crime Insurance Program is a "social program" rather than an insurance program. The Program is subsidized by the federal government in order that the premium may be affordable as required under the statute. To continue the Program, under this condition, it would be necessary for the Congress to appropriate some $50 million.

The lack of availability of crime insurance is not a national problem but an individual state problem. Even within the states the availability and affordability problem is confined to certain local areas within the state. The bulk of the policies have been issued in New York, Pennsylvania, Florida and Massachusetts. Approximately 77,000 policies are currently in force in 30 jurisdictions with 60 percent of the policies issued in New York.

In a state where a crime insurance availability problem has been demonstrated, a solution to that problem should be "tailor-made" to meet the needs of constituents in that state. The Alliance is willing to help establish an effective program in those communities where a problem exists, we are committed to working with state administrations towards this end. The Alliance Property Insurance Committee at its February 1983 meeting recommended that the Alliance staff draft legislation implementing a state crime insurance program and submit it to the Committee at its September 1983 meeting. The legislative draft would be used only in those states where a demonstrated need for a crime insurance program existed following expiration of the federal program. The Alliance Property Committee believes that state crime insurance programs would not be widely needed because the current federal program has a substantial number of policies only in a few states and that upon the expiration of the federal program the private market would in most cases insure the business through the voluntary market.

C. National Flood Insurance Program

The National Flood Insurance Program was established under authority of the National Flood Insurance Act of 1968. It is a subsidized government supported program designed to help owners of real or personal property in areas designated as eligible for flood insurance, purchase such insurance.

The Alliance and NAMIC have been strong supporters of the National Flood Insurance Program. We urged our member companies to fully support the development of the Program, to promote the sale of flood insurance policies, to offer claims and other service expertise and to participate with government as risks-sharing partners. Today, we urge reauthorization of the National Flood Insurance Program until September 30, 1985.

During the first ten years of its existence (1968-78), the National Flood Insurance Program operated as a partnership between the private industry and the federal government. In spite of the success of the co-operative program, the Federal Insurance Administration, for reasons of its own, decided to dissolve the partnership. FIA on January 1, 1978, began to operate the program unilaterally. Abrupt termination of the agreement between FIA and private insurance companies created extensive dislocation among companies which, in good faith, had established special servicing units. Many employees had to be terminated making the government action very costly to participating companies.

The present Administration has expressed an interest in establishing a working relationship with the private industry under the National Flood Insurance Act. The Alliance and NAMIC have been working with the FIA in an effort to help make the National Flood Insurance Program operate on a more business like basis. For more than a year, we have been meeting with the Federal Insurance Administrator to explore the feasibility of renewed industry participation in the operation of the Program. Presently, the insurance industry and the government are developing a "write-your-own" program. The "write-your-own" program seems to be a feasible approach by which private insurers would market the flood insurance policy to its present policyholders. It is estimated there are eight million potential flood insurance policyholders, however, the present marketing system only reaches 25 percent or two million policyholders. It is contemplated that with industry marketing the flood policy, inroads to this total market can be achieved.

The goal of the Federal Insurance Administration is to minimize direct federal involvement in the Program. FIA has encouraged participation by the private insurance industry in the "write-your-own" program. FIA has also sought input from the industry as to alternatives which would improve the operations of the Program. The objective is to identify problems so that steps can be taken to mitigate as many of the problems as possible, thereby creating a climate in which the industry can participate. Several insurance companies have looked on the "write-your-own" as a positive step in the right direction.

In summary, the Alliance of American Insurers and the National Association of Mutual Insurance Companies recommend that the Subcommittee extend the National Flood Insurance Program to September 30, 1985, and discontinue the Crime Insurance and the Riot Reinsurance Programs as of September 30, 1983.

We thank you for this opportunity to present our views and will be pleased to answer questions.

Senator HECHT. Thank you, Mr. Jones.
Mr. Fritzel.

STATEMENT OF CHARLES H. FRITZEL, ASSISTANT VICE PRESIDENT FOR GOVERNMENT RELATIONS, NATIONAL ASSOCIATION OF INDEPENDENT INSURERS

Mr. FRITZEL. Thank you, Mr. Chairman. My name is Charles H. Fritzel, and I am the assistant vice president for Government relations of the National Association of Independent Insurers, a voluntary national trade association of over 530 insurance companies.

[The complete statement follows:]

STATEMENT OF
CHARLES H. FRITZEL
ASSISTANT VICE PRESIDENT FOR GOVERNMENT RELATIONS
NATIONAL ASSOCIATION OF INDEPENDENT INSURERS
BEFORE THE
SUBCOMMITTEE ON INSURANCE
OF THE
BANKING, HOUSING, AND URBAN AFFAIRS COMMITTEE
UNITED STATES SENATE
APRIL 8, 1983

My name is Charles H. Fritzel and I am the Assistant Vice President for Government Relations of the National Association of Independent Insurers (NAII).

NAII favors termination of the Federal Riot Reinsurance Program and the Federal Crime Insurance Program. We support a viable National Flood Insurance Program.

NAII is a voluntary national trade association of over 530 insurers. Our organization provides a truly representative cross section of the property and casualty insurance business in America. Our members range in size from the smallest one-state companies to very large national underwriters, and consist of both stock and non-stock companies. NAII member companies reflect all forms of merchandising -- independent agency, exclusive agency, and direct writers; and they include insurers which serve a general consumer market and those which specialize in serving particular consumer groups such as farmers, teachers, government employees, military personnel, and truckers.

Federal Riot Reinsurance

NAII believes the need for the Federal Riot Reinsurance program no longer exists. In the past, the artificially low rate of 2.5 cents per 100 dollars of subject premium attracted many insurers to the program because it was below the private market cost. On October 1, 1981, the Federal Insurance Administration (FIA) increased the reinsurance rate by tenfold to 25 cents per 100. This was done, in part, to rebuild the National Insurance Development Fund which had been depleted by payments of crime insurance losses. The effect of the rate increase was to make the program competitive with the private reinsurance market.

We understand that 19 insurers currently are purchasing the federal riot reinsurance in the 15 states where it is available. This represents a significant decline -- down from 98 in January of 1982 -- and demonstrates to our satisfaction that private reinsurance can provide this coverage.

The ability of state regulators to assure the continued availability of property insurance through FAIR Plans and the ability of private insurers to provide backing for insurers participating in the FAIR Plans is now a fact. The Riot Reinsurance program has served its purpose and need not be renewed.

Federal Crime Insurance Program

The Federal Crime Insurance program is not insurance. It is a subsidy to businesses and residents of high crime areas. In the twelve months from March, 1982, through February, 1983, the program paid out over $22 million on just under 8,000 claims. It took in premiums of about $13.5 million. This leaves a deficit of $8.5 million.

The crime insurance program is not dependent upon the premiums from the Riot Reinsurance program in order to pay losses. There is no reason to tie the two programs together. It is true that riot reinsurance premiums are paid into the National Insurance Development Fund which, in turn, pays losses for both programs. But with so few insurers participating in the riot reinsurance program, the Fund has virtually dried up. It is our understanding that the FIA is now using its borrowing authority at the Treasury to pay crime insurance claims.

In 1982 there were approximately 71,000 crime insurance policies in force. Today, that figure has dropped by about 11,000 policies to just under 60,000. This drop in policyholders reflects changes which the FIA has made in the program, including an increase in premium and elimination of coverage above $500 for jewelry and furs. I think it can be said that the decline in the number of policyholders reflects what a bargain this program has been. Why pay more for private coverage when you can buy subsidized insurance from the federal government? But when the rate went up and the coverages were tightened, then it became less attractive to a great number of insureds.

The program can hardly be called national in scope. Nearly 80 percent of the current policies are written in just five states -- nearly 60 percent in New York State with 35,000 policies in force. Pennsylvania is second with 4,200, then Florida with 3,300, New Jersey with 2,400 and Massachusetts with 2,000.

NAII believes this is a program which the states should take over, primarily because it is concentrated in just a few states and is not very large. Alternatives to the federal program are available. Michigan, New Jersey, Indiana and Wisconsin have varying types of crime insurance programs. Neither Michigan nor Indiana participate in the federal program. Rhode Island, Wisconsin, Michigan, Maryland and Illinois have added crime insurance coverage

through their FAIR Plans. States have created residual market mechanisms for high risk automobile drivers and homeowners whose property may be uninsurable at "affordable" rates in the private market. The same could be done for crime insurance.

Insurance is a state regulated business and because we believe in state regulation and because so much of the program is concentrated in just a few states, we think it is better to let the states address the question of crime insurance.

Mr. Chairman, you asked us to comment in detail on the role of the private sector in meeting the needs of the areas affected by the civil disturbances in Miami. As a result of the May, 1980 disturbance in Miami, the insurance industry paid out $65,250,000 in claims. To the best of our knowledge, the industry has not withdrawn from the Miami market. The fact that there have not been many complaints about the availability of insurance in Miami demonstrates that there is not a major availability problem in Miami. The agents we spoke to have assured us that insurance is available in Miami. The insurance industry met its obligation following the 1980 riots and continues to meet its obligations today. I am sorry I cannot provide more detail, but the fact is, there just is not a great deal to say. Insurance is being written in Miami today and losses incurred under those policies are being paid.

National Flood Insurance Program

NAII supports a strong and viable National Flood Insurance Program and we favor its renewal. We wish to commend FIA Administrator Jeff Bragg for his efforts in putting the program on a more businesslike basis. Mr. Bragg has met with industry representatives in an effort to keep us informed of his plans for the program. He is developing a plan by which private insurers could market and service national flood insurance right along with their regular homeowner's coverage. We look forward to continuing this spirit of cooperation.

Thank you.

Senator HECHT. Thank you.
Mr. Nutter.

STATEMENT OF FRANKLIN NUTTER, REINSURANCE ASSOCIATION OF AMERICA

Mr. NUTTER. Mr. Chairman, I will be brief in the interest of time.
[The complete statement follows:]

STATEMENT OF THE
REINSURANCE ASSOCIATION OF AMERICA
CONCERNING THE
FEDERAL RIOT REINSURANCE PROGRAM
APRIL 8, 1983

The Reinsurance Association of America is a trade association representing professional property and casualty reinsurers in the United States. Reinsurance is the business of one insurer assuming all or part of a risk originally undertaken by another insurance company. A professional reinsurer is an insurance company which has as its principal activity the writing of reinsurance and is to be contrasted with insurance companies which directly insure the general public. The RAA's member companies assume more than $4 billion of gross reinsurance premiums annually.

The origin of the Urban Property Protection and Riot Reinsurance Act of 1968 lies in the widespread social disturbances of the 1960's. During that period, these serious conditions and uncertainties raised questions as to the continued availability of property insurance in urban areas. The Congress responded with the enactment of a program which authorized the federal government to offer riot reinsurance to insurers in those jurisdictions which enacted laws assuring the availability of property insurance for those unable to obtain it in the private market. In many cases, state legislatures elected not to participate in the Program or meet federal requirements. Federal riot reinsurance has not been available in those jurisdictions.

Even in those states in which the federal government now offers riot reinsurance, most primary insurers do not participate in the Program. In those cases insurers have concluded that adequate protection, competitively priced, from the private reinsurance market is available. Moreover, many reinsurers believe that the Program is unnecessary or improperly structured.

Requests have been made at times to compare riot reinsurance coverage available in the private market with the federal Program. It is difficult to make such a comparison because no private reinsurer offers coverage identical to the federal contract. The federal program can be described as an aggregate excess of loss reinsurance treaty providing coverage on specific lines of insurance; such as fire and extended coverage, other allied lines of fire insurance, and burglary and theft for losses arising from defined conditions of civil disorder in excess of a predetermined retention based on a company's previous year's premiums in each state. A company's aggregate retention in each state is five percent of direct premiums earned for covered lines in that state with a $1,000 minimum. Thus, in the case of an insurer having earned premiums of $1 million in a state, the retention would be only $50,000. Above this level, the federal plan could pay at least 90 percent of all losses incurred in the state resulting from the event.

In contrast, the private reinsurance market offers an excess of loss treaty providing protection against losses in excess of a predetermined retention <u>per risk</u> resulting from a

number of perils, including riots. In the private market retentions are not determined on a state-by-state basis. Instead, an insurer's retention will be determined by its total capacity to retain a portion of the risk. The private market also offers catastrophe cover to protect primary insurers from the accumulation of individual losses arising from a single event.

These disparities in the method by which coverage is obtained in the federal Program as contrasted to the private market make it impossible to compare rates. However, it is clear that adequate reinsurance is readily available in the private market at reasonable rates. This availability in the private sector explains the mass exodus from the federal Program in recent years. The withdrawal has resulted in a reduction of coverage in force in the federal Program from the last contract year, even though the Program experienced an 88% reduction in coverage in the 1981 contract year.

The Federal Riot Reinsurance Program was introduced because the coverage was thought to be unavailable in the private market although it was presumed needed to make necessary property insurance coverage available. To the credit of all involved, most states enacted FAIR plans to provide essential property coverage at reasonable rates. Today the states and the insurance industry are committed to the continuation of essential property insurance through FAIR plans.

Whether truly needed at the time or not, the Federal Riot Reinsurance Program served as a catalyst for the creation of these essential insurance mechanisms. It is important to know, however, that the existence of the Federal Riot Program is not a legal or economic condition for the continuation of these FAIR plans. Moreover, there is no evidence that property insurance availability is enhanced by the presence of the Federal Riot Reinsurance Program. In fact, the mere showing that only a small fraction of the qualifying companies buy the federal coverage is ample evidence that it does not affect coverage in today's marketplace.

In conclusion, the Reinsurance Association of America recommends that the Federal Riot Reinsurance Program not be continued. While it is impossible to guarantee unlimited capacity or state unequivocally that future availability will always be adequate in the private market, present circumstances demonstrate that the federal Program is no longer needed to assure availability of essential property coverage.

# # #

Senator HECHT. Thank you for the brief summary. I appreciate it very much.

I would just ask a few questions.

Superintendent Corcoran, according to the most recent records of the Federal Insurance Administration, there are 34,123 FAIR plan policies in New York State, 25,214 of which are residential and 8,909 commercial. If the FAIR insurance availability problem in New York State can be handled so effectively through an entirely State regulated mechanism, why should the crime insurance availability problems of 34,886 New Yorkers have to be handled by the Federal Government.

CANNOT AFFORD INSURACE RATES

Mr. CORCORAN. Well, first of all, as I said in my testimony, New York has actively outreached the public making it aware it's available. I don't think reading these figures you can deduce there's no need for a Federal crime insurance program. I'm amazed at the testimony that when they raised the rates people stopped buying the product. The thing is aimed at people who can't afford the open market situation. What we're looking at here—nobody is disagreeing—if we could prove here there's adequate and affordable insurance coverage for people who are in a destitute situation that would be wonderful. We wouldn't need the program. But the facts are proven that there is not adequate and affordable coverage.

The testimony that when they raised the premiums that people dropped the policies just simply proves that the people who are buying the policies cannot afford them now.

Now as far as the regional response, because New York benefitted through outreach should not be reason for stopping the Federal program. We're not saying we should stop the Federal flood program or earthquake programs or other things that help other sections of the country.

I think the thing here is, is there something in place now to help these people; and the answer is there is not. And as far as commercial availability, I see the industry speaks to itself and not to the real world that I see. There is not adequate affordable insurance out there for the people who need it in these areas. If this program was discontinued that phenomenon would cause an upheaval. In places like Brooklyn and other places of high risk, you don't go in and sell them insurance. So the real situation is there would not be adequate coverage available.

Mr. FRITZEL. Mr. Chairman, could I comment on that question also?

Senator HECHT. Yes.

Mr. FRITZEL. We are not arguing with the superintendent over the question of availability of crime insurance. He quoted a rate of $220 in his testimony. That rate is actuarially sound and it is above the rate that the Federal program is now charging. Perhaps he's correct in saying that private insurers would even want to charge more. Some would and some might not.

WHO WILL SUBSIDIZE INSURANCE?

I think where our difference lies is in who is going to pay the subsidy for crime insurance. Is it going to be the Federal Government or is it going to be the State of New York by developing its own plan, a plan which we will assist in developing. We will cooperate with them whether it's legislatively, administratively, or any other way. Other States have done it and the State of New York can do it. I think the State of New York is to be commended, if, in fact, they have gone out and made known the existence of this Federal crime insurance program.

But the real point I think is the one we are trying to make, who is going to pay the difference? Is it going to be the taxpayers of all the United States or the taxpayers of the State of New York where the losses occur?

And I also—as long as I've got the microphone—would like to say that I don't think it's fair to compare the flood insurance program with the crime insurance program. The flood insurance program is a very large program, almost two million policies are being written there. There are about 60,000 crime insurance policies. The losses that occur in the flood program often include a person's life savings in the form of their house being washed down the river or something like that. The losses in the crime insurance program are easily replaceable items, so there are differences.

Mr. CORCORAN. Could I respond to the easily replaceable items? This program is aimed at people who cannot replace those items. The fact of the matter is, why should the Federal Government chip in? Simple. This benefits the depressed areas we have throughout the Nation. With the Federal crime program in existence and people knowing about it and keeping the inner-cities, we are not the only city in the country that has crime problems. So if they have this availability in this commercial line especially, they will keep a good nucleus of a good economy in each of these areas.

Senator HECHT. Thank you. Mr. Fritzel, I'm from Las Vegas, the show biz capital, and the first rule of show biz is those who have the mike have the mike.

Getting back again, Mr. Commissioner, there are 25,677 residential Federal crime insurance program policies and 9,209 commercial Federal crime insurance policies in effect in New York. These figures are almost the same as those for your State's FAIR plan. If crime was added to residential FAIR plan policies, would that not almost overnight resolve the crime insurance availability problem for the vast majority of the Federal crime insurance program policyholders in New York State?

Mr. CORCORAN. Well, I either missed something or the logic of just adding those. They are not the same people. They're not the same constituents.

Senator HECHT. Are they?

Mr. CORCORAN. Not to my understanding. They are not. These are the people who buy commercial lines in commercial inner-cities who cannot get insurance.

Senator HECHT. How many would you feel would be included in that?

Mr. CORCORAN. Well, the figures that I have been shown by my people, what would happen in the residential situation is they could get private insurance carriers. But as far as the commercial, we don't see any industry clamoring through those areas insuring people. The program benefits more directly the small commercial establishment in those areas and there's no industry clamoring to go in and write these at reasonable rates that people can afford.

Senator HECHT. Given the existence of the FAIR plan, why would it not be possible to achieve the State solution within say the next 6 months; that is, if there's a need for action by the State legislature, could you do that?

Mr. CORCORAN. I don't have the answer to that question. Could we do it in the next 6 months? I doubt it.

Senator HECHT. One last question to you. It was brought out to me that you're new to your job as superintendent of insurance of New York and I want to congratulate you on your confirmation.

Mr. CORCORAN. Thank you.

Senator HECHT. You mentioned after your testimony that improvements were possible in the crime program. Could you in the near future submit to this subcommittee some details of improvements that you suggest?

Mr. CORCORAN. My suggestions directly—this is aimed at people who are unable to obtain adequate and affordable coverage and those are the people that this should be made available to. I'm sure this is available to people who can afford this product. The product was not designed for the affluent. Also making sure when they buy it that they show that they cannot afford the other.

Senator HECHT. Would you give us a written statement on that and we would appreciate it very much.

Mr. Nutter, in his testimony Mr. Bernstein suggests that even though private market riot reinsurance is available we should keep the program in place just in case of a recurrence of major civil disturbances. Could you comment on this?

Mr. NUTTER. Mr. Bernstein's written statement also suggests that the companies are much better prepared for the incidence of riots in the future. We don't feel that the program is necessary. Mr. Bernstein says that the reason companies are not purchasing coverage from the Federal program is because of price. It suggests that what's going on here is rate shopping. I don't think the Federal program was created for that. The private companies are fully capable of responding and of providing this coverage in the private market. We don't see any reason why there would be any retrenchment and in fact the evidence in Florida, for which the Federal program does not provide riot reinsurance, is to the effect that the private riot reinsurance coverage has not been withdrawn, has not been replaced, and is not difficult to obtain.

Senator HECHT. Mr. Jones, the Urban Property Protection and Reinsurance Act of 1968 authorized the Federal Government to provide crime insurance at an affordable rate where there existed a problem of availability.

In advocating the termination of the program, are you suggesting that private industry will be subsidizing an affordable program?

Mr. JONES. No, Mr. Chairman. We are suggesting that private industry is willing to work with those States that have a critical

crime availability problem to work out a program for the high-risk areas. It may be possible that some of those insured within the crime program now in those areas may be written in the private market, but for those who would not qualify for private underwriting procedures, we are willing to sit down with that State. I think, as Mr. Fritzel was saying, it's a decision as to who's going to pay the subsidy for the high-crime areas and the high-risk areas. More than likely to have a subsidy will be necessary. Who's going to pay the subsidy, the State or the Federal Government is the question.

We think the States should be involved in the subsidy and are willing to sit down and work with those State administrators to work out a feasible program, like has been done in other areas.

Senator HECHT. The Commissioner would like to comment on that.

Mr. CORCORAN. I assure you the State budgets are facing the same problem as the Federal budget is facing and if the industry is so anxious to write the business I would be glad to sit down with the industry. If they want to write the good business, maybe they can write the bad business and maybe there's no need for a subsidy.

Mr. BERNSTEIN. I would just like to point out on behalf of the American Insurance Association that we are not as self-sacrificing as some of my colleagues on my left. We recognize that had the losses from the Federal crime insurance been absorbed in FAIR plans and by private insurers the industry would have eaten another $150 million in losses over the life of this program.

This was set up as a social program. We agree it is a social program. We do not believe an insurer should sell insurance above cost, but they are required to take into consideration actual losses and expenses and, if that were true, the premiums charged would have to have been at least $150 million more than were charged by the Federal crime insurance program. That would clearly not have permitted the insurance to be affordable to the people who need it.

As to affordability, my understanding is that the program for commercial use is still set up on the basis of gross receipts. So the smaller your gross receipts, the lower your premiums. This makes the insurance program unaffordable for well-off risks right now in the commercial area. So that concern is already taken care of by the very nature of the program. Sears Roebuck would have to pay ten times as much to the Federal Government for crime insurance than it would to a private insurer. A "Ma and Pop" grocery store in a high-crime area that would go out of business and to whom a heavy crime loss is just as devastating as the loss of a home to someone in the flood program, those people need this program on the lower prices set based on their gross receipts.

Senator HECHT. Mr. Jones, you indicate that your association is poised and willing to assist State administrations in setting up an appropriate mechanism for providing crime insurance. Could you elaborate?

Mr. JONES. Our staff has been directed by our insurance committee to work out a feasible program. This was just done in February and we don't have the prototype developed, but we do plan to have it available by September, Mr. Chairman.

Senator HECHT. Several witnesses have suggested that the Federal crime insurance program is necessary for the continued revitalization of our urban centers. Do you agree with this statement?

Mr. JONES. Not totally. I do have some exceptions to that statement.

Senator HECHT. Do you want to elaborate briefly?

Mr. JONES. I will provide that for the record to you, Mr. Chairman, if that would be all right.

Senator HECHT. Thank you very much.

[Information supplied for the record follows:]

Alliance

Washington Office

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1110 Vermont Avenue, N.W.
Washington, D.C. 20005
202-822-8811

April 11, 1983

The Honorable Chic Hecht
Chairman
Senate Subcommittee on Insurance
Committee on Banking, Housing and
Urban Affairs
Room SD534
Washington, D. C. 20510

Dear Mr. Chairman:

You directed the following question to me during the Q and A session of the oversight hearing held by your Subcommittee on Friday, April 8th: "Several witnesses have suggested that federal crime insurance is necessary for the revitalization of urban centers. Do you agree?"

Our answer to the question is "No." The Federal Crime Insurance Program is not necessary for the revitalization of our urban centers. However, crime insurance and insurance generally are important to the revitalization of our urban centers. A federal program is not needed to provide the essential insurance. We testified that the federal program should be discontinued and the states should establish their own program.

Insuring of the crime peril is directly affected by the degree to which law and order are maintained. In combination with other measures, crime insurance will help to improve the conditions of our inner cities but is not the sole factor. Insurance is only one of the basic forces needed in efforts to revitalize urban centers.

I would like to call your attention to an article in the July 7, 1982, Wall Street Journal (copy attached). We asked our New York office to check with some of the businesses in the Local Development Cooperation of East New York. The results of a random sample indicated that several of the businesses were not aware of the Federal Crime Insurance Program or did not participate in the program. The point is that programs like the one in East New York will improve the availability of private crime insurance.

A subsidized federal crime insurance program does not prevent crime. If programs were supported to prevent crime, insurance availability would not be a problem. A national program should not be used to solve the problems of an individual local area.

We thank you for the opportunity of presenting our views on this issue. If you have any questions, please contact me.

Sincerely,

James E. Jones, Jr.
Government Affairs Representative

JEJ:lbd
Enclosure

Copy to: G. Wyrsch

[From the Wall Street Journal, July 7, 1982]

THE JOB KILLER

Three years ago, Larry Rose was about to move his wholesale hardware business from East New York, a rundown inner-city section of Brooklyn, N.Y. He was born in the area, and had run the business there since 1935, but he didn't think he could afford to stay, because his 20-employee warehouse was being burglarized almost every other week. Not only was he losing goods, but he was forever having to repair the part of the building that was broken into, his insurance premiums were skyrocketing and he was having trouble meeting deliveries to customers. So Mr. Rose was actively scouting warehouse properties in the Long Island suburbs.

But instead of leaving, Mr. Rose joined a group of businessmen who decided to reverse the exodus of industry from the area. They formed the Local Development Corp. of East New York (LDC), which set up a 40-block industrial park with the help of public funds and private contributions. To retain businesses—and attract new ones—they decided their top priority would be to stamp out crime.

In the early 1970's, some 200 businesses employing over 3,000 people were operating in the 40-block area. But by 1979, only 45 were left, employing about 1,500. The overwhelming reason that businessmen gave for leaving was crime: They were fed up with burglaries, and sick and tired of having their employees mugged as they walked to or from work.

To combat crime, the LDC took several steps. It knocked down all abandoned buildings in the 40-block area—there were 1241—removing an ideal lurking place for street hoods and burglars. It put in street lights and installed better security devices at individual businesses. This year it started up an eight-man security patrol, whose operating expenses are paid by the local businessmen. One of the patrol's major purposes is to respond to alarms and alert the police if there is trouble; previously there had been so many false alarms that the police usually didn't bother to respond.

The results have been astonishing. In 1980, there were 134 burglaries and 208 robberies in the 40-block area. By 1981 that had dropped to 27 burglaries and 75 robberies. This year, based on seasonably adjusted first-quarter figures, the LDC expects 20 burglaries and 20 robberies.

It's too early to tell whether the drop in crime will bring industry and jobs back to East New York. All but one of the 45 businesses in the area in 1979 have remained, and a couple of new firms have moved in. Mark Cabinet Corp., which makes filing cabinets and employs 60 workers, put in a new warehouse and says its sales volume is up 40 percent over last year.

But it's worth paying attention to the crackdown on crime in East New York, and other community actions like it across the country. It could well be that one of the most effective ways of lowering unemployment in inner cities is to make it safe for businesses to operate there.

Senator HECHT. Mr. Fritzel, are there any members of your association participating in the riot reinsurance program and, if so, how many?

Mr. FRITZEL. Yes, there are. I'd have to check the list. I think there are maybe three or four companies. I can supply the names of those companies for the record.

Senator HECHT. Please. Is the Federal Insurance Administration playing any role in assisting these companies?

Mr. FRITZEL. I beg your pardon?

SUGGESTIONS TO INSURERS IF CONGRESS TERMINATES RIOT PROGRAM

Senator HECHT. I'm sorry. What are you suggesting to these insurers in the event that Congress terminate the riot program?

Mr. FRITZEL. We would suggest that they seek coverage from a private reinsurance program.

Mr. CORCORAN. Seek coverage at what rates and just seek coverage is a very vague question. It's a typical phenomenon of the industry to write the good and rich and disregard the high risk people, so to seek coverage is very broad.

Mr. FRITZEL. They would have no choice. They would look for coverage and find it in the private reinsurance market at whatever rate they can negotiate. Perhaps Mr. Nutter can speak to that.

Senator HECHT. Gentlemen, I've enjoyed this panel better than any. It's good. Do you want to speak on that, Mr. Nutter?

Mr. NUTTER. I would just add that there certainly appears to be no problem with the coverage. The Superintendent may have been responding to the comment in the context of crime insurance program but the question was in the context of the riot reinsurance program. I said before that there was no real ability to compare rates but I think that there's no question that riot reinsurance is readily available in the private market at very affordable rates.

Senator HECHT. Mr. Bernstein, I see you want to comment on that last answer.

Mr. BERNSTEIN. Yes; I think the American Insurance Association companies agree that riot reinsurance is currently available at affordable rates privately and that the Federal price is too high and it's not a question of price shopping, but that situation could change. In 1963, the riot reinsurance was easily available. The Rochester riot occurred in 1964 and things began to get a little tight. You had the Watts riot following and by the time of the D.C.-Newark-Detroit riots there was no riot reinsurance available in the private market and the companies came down to Washington hat in hand begging for a riot reinsurance program. The price to be paid was the establishment of FAIR plans to provide insurance privately. That could happen tomorrow. The fact that we all survived happily the Miami riots does not mean that we could survive a number of similar riots, and if the riots tended to accelerate around the country why should we have to come back for a new Federal program when right now, even on the basis of current premiums, the Federal Government is taking in more money to cover its riot losses than it's paying out? Last year it took in $600-odd thousand in premiums and paid out zero in losses, paid out $111 thousand in expenses, and made a $500,000 profit. It's made $120 million profit over the life of the program. The riot program has cost the Federal Government not a penny. If the companies don't want to buy it, they don't have to buy it. Nobody is forcing them to, but some companies feel they need it. That program should continue for those companies and the program should continue as inexpensively as it exists on the books so that, God forbid, if we had a series of riots and the riot reinsurance market dries up privately, we have a Federal insurance program and we don't have to reconstitute it.

Senator HECHT. One last question for Mr. Fritzel. Does the high incidence of crime itself support the need for a Federal crime program?

STATE REGULATION OF INSURANCE

Mr. FRITZEL. I will say no to that in that so much as you say Federal crime insurance program. I think that in some States there is a need for some kind of residual market mechanism to handle crime losses and that's what we're talking about—State regulation of the insurance business. We are a State-regulated business an[illegible]

we're willing to take whatever the State is going to give us. We hope we can help them in developing something. We may not like what they give us, but we in our association are willing to face that at the State level. We would much rather deal with Mr. Corcoran than we would with Mr. Bragg.

Mr. CORCORAN. Senator, could I get that in writing? This is wonderful.

Mr. FRITZEL. We have talked to the New York State Senate Insurance Committee Chairman, Senator Dunn I believe his name is, and we know there are some special problems in New York. It's the city against the rest of the State. But we hope we can help them solve those problems and when they come up with a solution we're willing to work with that.

Mr. JONES. And we're saying the same thing, Mr. Chairman.

Senator HECHT. I think we should compliment Mr. Gerry Wyrsch for bringing you all together and maybe we can work it out right here.

Mr. Bernstein, if the Congress in the late 1960's and early 1970's had been able to look into the future and see that the Federal crime insurance program would only be benefitting about 59,000 policyholders, do you think they would have established such a program?

Mr. BERNSTEIN. I think given the history of the particular program and the fact that it was established at the initiation of Congressman Annunzio of Chicago who was concerned with the key availability problems in Chicago, that Congress looked at the fact that there were key urban areas that had the problem. It didn't quantify the need. I think that the fact that the program is not marketed accounts to some extent for the lack of more. If we had less than 59,000, somewhat less, the program clearly would be less national in scope. I don't know where the cutoff number is. If you look at the relative need in areas like New York and in areas like Florida and areas like Massachusetts and Pennsylvania, you may have 5,000 policies in some of those States; you may have 3,000; but those are 3,000 people who might not be in business without this program and that might be a further drain on the economy as well as not having the right to make their own living. I know in D.C. when this program came in there were people who for the first time could get consignments for things like TV goods in their stores because of this program. They couldn't have been in business without it. To those people this is an essential program.

I believe this Congress may or may not have expected a larger number but Congress did not establish the program based on the target number but on the basis of need in key areas knowing there would not be a truly national program. In fact, the language of the statute points out the Administrator had the obligation to determine which States need it which clearly bespoke the fact that Congress knew that all States wouldn't need it.

But again, as the Commissioner of New York pointed out, almost 70 percent of the flood program comes from policies in three States. That's even a higher proportion than those that are in the crime program from three States.

The point is, you don't measure this by number. You measure it by need.

If Congress decides that crime insurance is no longer a social need, then the program ought to be eliminated. But I would hate to see Congress decide it's not a social need at the Federal level and then have Congress urge the States to impose a similar program at the State level knowing that the States do not have the subsidy moneys to come up with and, frankly, on behalf of my companies, we don't want to eat that $150 million when we're forced to sell insurance below costs, which is what this program requires. If we were permitted to sell crime insurance at the actuarial rate, we wouldn't lose money, but then nobody would buy the insurance. But if this is a social program, then some government has the responsibility to pay the bill. I don't think the States can do it now and I think the Federal program is run efficiently and it's been reviewed by GAO as being a very efficient operation, and I think it's the best way for it to be continued.

Senator HECHT. You were at one time the Federal Insurance Administrator, were you not?

Mr. BERNSTEIN. Yes, I was.

Senator HECHT. Doesn't the low number of insurers in the current program confirm your own conclusion in your days as Insurance Administrator that these programs could be best handled at the State level?

PREFER STATE PROGRAM

Mr. BERNSTEIN. When I was involved in writing the Federal report that was required in 1970 to evaluate the need for a Federal crime insurance program, our report said there should not be a Federal program; there should be a State program but that a subsidy was required. The States responded to that and the insurance industry responded to that with an absolute backhand. The States, with very few exceptions, failed to establish programs and Congress said that's not enough; we need a Federal program. Therefore, Congress passed the Federal program.

I would personally prefer, based on my own philosophy, to see this handled at the State level. I know that's fiscally impossible, given the economic situation of the States. If they didn't do it in 1970 when they were in a far better financial situation than they are today, they're not going to do it tomorrow.

Mr. CORCORAN. Senator, if you have the States take care of this individually you're going to have sporadic and inefficient handling. I see this program as a national preventive medicine in the economic sense, even though a small amount. Those are the inner-city problems. And if you have this mechanism in place and the States properly publicize like we do, it will be there and it will be used. The inner-city problems are nationwide, not New York. New York just happened to have had a little more PR that we have an insurance program, but if you let it be sporadically handled and inconsistently, the benefit will be killed. It has to be preventive medicine at the economic level.

Senator HECHT. I have no further questions but because this has been a spirited debate which I have enjoyed, if each of you want to summarize your comments for the record in about 30 seconds I'll sure give you the opportunity to do so.

Mr. NUTTER. I have no further remarks. Thank you.

Senator HECHT. Mr. Fritzel?

Mr. FRITZEL. My major point today is that we favor State regulation of insurance and we would like to see elimination of the two Federal programs, the crime insurance and riot reinsurance programs, replaced where necessary at the State level.

Senator HECHT. Mr. Jones.

Mr. JONES. The Alliance supports State regulation of insurance. We believe that where it is not necessary for the Federal Government to get involved in the insurance business that they should not be in the insurance business.

Senator HECHT. Mr. Bernstein.

Mr. BERNSTEIN. I have no argument with the last statement philosophically. My concern is that it doesn't apply to the facts. We're not talking about State regulation of insurance here. We're talking, quite bluntly, about money, and where these subsidies are going to come from. In crime insurance, that subsidy has got to come from the Federal Government or there will be no subsidy.

With respect to the riot reinsurance, that again is not a regulatory issue. It's a question of potential Federal backup for severe catastrophic losses in case of riot. The Federal Government made $120 million in selling that to private companies. The Federal Government made money and the private companies got their value in terms of security. The availability of that security is what we urge the Congress to continue.

Senator HECHT. Thank you. You're last, Commissioner.

Mr. CORCORAN. Senator, no one has proven that the program is not necessary and I'll sit down and send material showing that it is needed in the inner-cities. I'm very touched that everyone wants to come under my jurisdiction, but I don't want to build an empire. But I know for the good of the people of the State of New York this program should be continued.

Senator HECHT. Thank you. And I want to compliment Mr. Jerry Worth for arranging this hearing today.

The meeting is adjourned.

[Whereupon, at 12:45 p.m., the hearing was adjourned.]

[Additional material submitted for the record follows.]

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